TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1966

No. 637

NORTHEASTERN PENNSYLVANIA NATIONAL BANK & TRUST COMPANY, ETC., PETITIONER,

vs.

UNITED STATES.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR CERTIORARI FILED OCTOBER 7, 1966
CERTIORARI GRANTED DECEMBER 5, 1966

SUPREME COURT OF THE UNITED STATES

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INDEX

RECORD PRESS, PRINTERS, NEW YORK, N. Y., DECEMBER 28, 1966

[fol. A]

IN THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 15,249

NORTHEASTERN PENNSYLVANIA NATIONAL BANK & TRUST COMPANY, EXECUTOR UNDER THE WILL OF CLARENCE C. YOUNG,

v.

UNITED STATES OF AMERICA, Appellant.

On Appeal from the Order of the United States District Court for the Middle District of Pennsylvania.

Appendix to the Brief for the Appellant

[fol. 3]

IN THE UNITED STATES DISTRICT COURT

DOCKET ENTRIES

Date *Proceedings*

1963

Jan. 28, Complaint and demand for jury trial.

Jan. 28, Summons issued returnable 60 days after service. Copies of complaint (4), Summons and copies (4) handed to U. S. Marshal for service.

Jan. 28, J. S. 5

Feb. 4, Summons returned served 1/29/63, together with copy of complaint, on the U. S. Attorney, Scranton, Pennsylvania, and by certified mail on the Attorney

Date *Proceedings*

1963

General, Department of Justice, Washington, D. C. (MF&E $3.00.)

Mar. 25, Answer of defendant.

Apr. 11, Praecipe to place case on the Trial List for the October 1963 Term of Court at Scranton, Pa.

Oct. 8, Minute Sheet of pre-trial conference. USA orally moved for summary judgment. Plaintiff allowed 30 days to file any cross motions. Court will set date for argument thereafter. (N)

Nov. 7, Motion of defendant for summary judgment, and notice that motion will be brought on for hearing on [fol. 4] January 14, 1964, at 11:00 a.m. at Scranton, Pennsylvania, and Certificate of service thereof.

Nov. 7, Brief of defendant in support of motion for summary judgment.

1964

Jan. 29, Letter of Clerk to counsel of record fixing hearing on motion of defendant for summary judgment for Monday, March 16, 1964, at 11:00 a.m. at Scranton, Pennsylvania.

Feb. 24, Order of Court, continuing case from the October 1963 Term of Court to the March 1964 Term of Court at Scranton, Pennsylvania. (MHS) Copies mailed to counsel of record.

Mar. 12, Motion of plaintiff for summary judgment, and Notice that said motion will be brought on for hearing 3-16-64 at 11:00 a.m. at Scranton, Pa.

Mar. 16, Minute Sheet of Clerk re hearing on Motion of plaintiff and defendant for summary judgment. Motion argued. Defendant allowed 15 days to make answer. (WJN).

Date *Proceedings*

1964

Mar. 16, Brief of plaintiff.

Mar. 30, Reply Brief of defendant in support of motion for summary judgment.

Aug. 10, Letter to counsel of record. Hearing on motions for summary judgment fixed for 8-14-64 at 11:30 a.m. at Scranton.

Aug. 14, Minute Sheet of Clerk, re hearing on cross motions for summary judgment. Supplemental briefs to [fol. 5] be filed and then Court will take motions under advisement. (N) Case continued to the Oct. 1964 term at Scranton.

Sept. 28, Supplemental Brief of defendant in support of motion for summary judgment.

Sept. 30, Memorandum of Judge Nealon, and Order: Now, this 30th day of September, 1964, in accordance with the Memorandum this day filed, it is hereby Ordered and Decreed that plaintiff's motion for summary judgment is entered in favor of the plaintiff and against the defendant in the amount of $17,574.45 with interest, as provided by law. Defendant's motion for summary judgment is denied. (N) Copies of memorandum and order mailed counsel of record.

Sept. 30, J. S. 6.

Nov. 27, Notice of Appeal filed by USA. Copies of Notice of Appeal mailed to counsel of record and to the U. S. Court of Appeals.

Dec. 1, Receipt for Notice of Appeal.

Dec. 24, Order that the time to docket the appeal and file the record with the U. S. Court of Appeals for the Third Circuit from the final judgment entered in this action, is extended for a period of fifty days from January 6, 1965 to February 25, 1965. (N) Copies

Date *Proceedings*

1964

of order mailed counsel of record and the U. S. Court of Appeals.

Dec. 30, Card from U. S. Court of Appeals acknowledging order extending time for filing and docketing record.

1965

Feb. 12, Record on Appeal mailed to U. S. Court of Appeals.

[fol. 6]

IN THE UNITED STATES DISTRICT COURT

COMPLAINT—Filed June 28, 1963

1. The Petitioner above named is the Executor of the Will of Clarence C. Young, a resident of the County of Lackawanna, who died testate on May 3, 1958 (a copy of the Will is herewith attached, made a part hereof, and marked Exhibit A), leaving to survive him a widow and four children, two of whom were sui juris.

2. This action arises under the Internal Revenue laws of the Defendant, the United States of America, and is for the recovery of taxes and penalties erroneously and illegally assessed and collected without authority from the Plaintiff, the Northeastern Pennsylvania National Bank & Trust Company, together with interest thereon. ~~The~~ deceased, Clarence C. Young, was a citizen of the United States, and at the time of his death resided within the jurisdiction of this Court.

3. Jurisdiction is conferred upon this Court by the provisions of Title 28, United States Code, Section 1346 (a)(1).

4. The Plaintiff's claim is for the recovery of $17,-574.45 representing taxes, penalties and interest assessed

and collected from the Plaintiff under Title 26, Section 2056, of the Internal Revenue Code of 1954.

[fol. 7] 5. The taxes, penalties and interest involved herein resulted from the interpretation by the Defendant, through its agents, servants and employees, of Item 6 of the last Will and Testament of Clarence C. Young, Deceased, which reads as follows:

> "Item 6: I give, devise and bequeath one-half (½) of all the rest, residue and remainder of my estate, whatsoever and wheresoever the same may be both real and personal, to which I may be entitled, or which I may have power to dispose of at the time of my death, unto my Trustee hereinafter named and designated, to have and to hold the same in trust, nevertheless, as hereinafter provided.
>
> (a) I direct my Trustee to pay out of the said income and corpus of the said estate unto my wife, Beatrice O. Young, the sum of Three Hundred Dollars ($300.00) per month for and during the period until my youngest child reaches the age of eighteen years, and thereafter I direct my Trustee to pay to my wife, Beatrice O. Young, the sum of Three Hundred Fifty Dollars ($350.00) per month for and during the rest of her natural life.
>
> (b) If my wife survives me, she shall have the power, exercisable by Will, to appoint to her estate, or to others, any or all of the principal remaining at the time of her death. If my wife fails to appoint the entire principal to her estate or to others as above authorized, then upon her death (or if she predeceases me, then upon my death) any principal remaining at that time shall be paid over to my children on the same terms and conditions as under Item 7 of this my Will."

[fol. 8] to the effect that the marital deduction was refused and denied the Plaintiff herein, resulting in the tax penalties and assessments hereinbefore set forth.

6. The Plaintiff avers that under the terms of Item 6 of the Last Will and Testament of Clarence C. Young his surviving spouse was given the marital deduction as the same is required and defined in Section 2056 of the Internal Revenue Code of 1954.

7. The Plaintiff avers that although Plaintiff met all the requirements of Section 2056 of the Internal Revenue Code of 1954, the Defendant unlawfully, erroneously and illegally assessed and collected from the Plaintiff the sum of $17,574.45.

8. On July 9, 1962, and simultaneously with the aforementioned payment of $17,574.45, Plaintiff filed with the District Director of Internal Revenue, Scranton, Pennsylvania, a claim for refund on Form 843 in the amount of $17,574.45, together with the statutory interest, asserting therein various alternative grounds as the basis of said claim. There is attached hereto, as Plaintiff's Exhibit B, a true and correct copy of said Claim for Refund, contents of which are incorporated herein by reference thereto.

9. On September 14, 1962, the District Director of Internal Revenue issued a Notice of Rejection of said Claim for Refund.

10. No part of the aforementioned $17,574.45 of assessment, penalties and interest thereon overpaid by the Plaintiff has been refunded to the said Plaintiff.

11. By virtue of the aforesaid, the Defendant, United States of America, became and is now indebted to the [fol. 9] Plaintiff for the full amount of $17,574.45, with interest, as provided by law.

Wherefore, the Plaintiff claims judgment against the Defendant in the sum of $17,574.45, with interest thereon, as provided by law.

Trial by jury demanded.

Alex Marcus, Donald Fendrick, Attorneys for Plaintiff.

Please Serve:

United States Attorney, Federal Building, Scranton, Pennsylvania;

Attorney General of the United States, Washington, D. C.

(Serve via Registered Mail)

Exhibit A to Complaint

LAST WILL AND TESTAMENT

BE IT REMEMBERED THAT I, CLARENCE C. YOUNG, of R.D. 1, Clarks Summit, in the County of Lackawanna and State of Pennsylvania, being of sound mind, memory and understanding, do make this my Last Will and Testament, hereby revoking and making void all other Wills and Testaments or writings in the nature thereof by me at any time heretofore made.

[fol. 10] ITEM 1. It is my will that all my just debts and funeral expenses be fully paid by my Executor hereinafter named, and that my said Executor provide, at the expense of my estate, and erect a suitable monument to perpetuate my memory in the minds of my family and friends.

ITEM 2. I direct my Executor hereinafter named to pay all inheritance, succession or transfer taxes, and all estate duties, which shall become payable by reason of my death out of the corpus of my estate.

ITEM 3. I give, devise and bequeath unto my wife, Beatrice O. Young, all my furniture, furnishings and fixtures, household goods and personal effects.

ITEM 4. I authorize and empower my Executor hereinafter named, whenever in the settlement of my estate it shall deem it advisable, to sell at public or private sale

all of my real estate, and to execute good and sufficient deeds or other instruments in transfer, and no purchaser at any such sale shall be bound to see to the application of the purchase money.

ITEM 5. I have entered into an agreement with my sons, Richard Young and George Young, for the purchase of all my capital stock in the C. C. Young Insurance Agency, Inc., of Scranton, Pennsylvania. In the event that I have not sold my capital stock in the said corporation to my sons as provided in the agreement entered into with my sons, Richard and George, during my lifetime, I direct and authorize my Executor hereinafter named to sell and transfer my said capital stock in the C. C. Young Insurance Agency, Inc., to my sons, Richard Young and George [fol. 11] Young, immediately after my decease in accordance with the terms and conditions of the said agreement entered into with them.

ITEM 6. I give, devise and bequeath one-half (½) of all the rest, residue and remainder or my estate, whatsoever and wheresoever the same may be, both real and personal, to which I may be entitled, or which I may have power to dispose of at the time of my death, unto my Trustee hereinafter named and designated, to have and to hold the same in trust, nevertheless, as hereinafter provided.

(a) I direct my Trustee to pay out of the said income and corpus of the said estate unto my wife, Beatrice O. Young, the sum of Three Hundred Dollars ($300.00) per month for and during the period until my youngest child reaches the age of eighteen years, and thereafter I direct my Trustee to pay to my wife, Beatrice O. Young, the sum of Three Hundred Fifty Dollars ($350.00) per month for and during the rest of her natural life.

(b) If my wife survives me, she shall have the power, exercisable by Will, to appoint to her estate,

or to others, any or all of the principal remaining at the time of her death. If my wife fails to appoint the entire principal to her estate or to others as above authorized, then upon her death (or if she predeceases me, then upon my death) any principal remaining at that time shall be paid over to my children on the same terms and conditions as under Item 7 of this my Will.

ITEM 7. I give, devise and bequeath the remaining one-half (½) of all the rest, residue and remainder of [fol. 12] my estate, whatsoever and wheresoever the same may be, both real and personal, to my children in equal shares, but in case either of them, or any of them, shall die in my lifetime leaving issue living at my death, such issue shall take by representation and per stirpes between them the share which his or her parent would have taken had such parent survived me.

ITEM 8. In the event that any of my children or their issue who will otherwise be entitled under the provisions of this my Last Will and Testament to share in any manner in my estate shall not at my death have attained his or her twenty-first (21) birthday, then I give, devise and bequeath any and all shares to which said person will be entitled unto The First National Bank & Trust Co. of Scranton, herein called my Trustee, in trust, to collect and receive such share, herein called the Trust Fund; to pay the net income thereof, and if the same is not sufficient, from the corpus of the said Trust Fund, a sum of not less than Fifty Dollars ($50.00) per month for the maintenance and support of said child until he or she reaches the age of twenty-one (21) years, and when such person shall have attained his or her twenty-first (21st) birthday, to pay over and transfer to him or her absolutely the corpus or capital of his or her share. In the event that such person shall die without having attained his or her twenty-first (21st) birthday, then in that event I direct my Trustee to transfer and pay over the said corpus or capital to the per-

son or persons who would, under the laws of the State of Pennsylvania, be entitled to his personal estate in case of his intestacy.

ITEM 9. I herewith direct my Trustee herein named, if any of my children during their minority shall attend [fol. 13] College or any graduate school, to pay for and on behalf of the education, maintenance and support of the said child so attending college or any graduate school, in addition to payments for support as provided for in Item 8, a sum not exceeding One Thousand Dollars ($1,000.00) during the entire school year the said sum or sums to be taken from income as well as corpus of the said Trust Fund whenever the same may be necessary, the same to be considered as an advancement and to be deducted from the respective child's share.

ITEM 10. In the event that any of my children shall have died in my lifetime without leaving issue, then his share shall be divided equally among the other children in equal shares, share and share alike, the shares to be distributed in accordance with the terms and conditions herein contained.

ITEM 11. The income and payments herein provided for my wife and children and the issue of my children are for their, and each of their, sole and separate use, maintenance and support, and are in no event to be liable for any debts contracted by them or any of them, and are not to be liable to attachment or assignment, but are solely and exclusively for their and each of their sole and individual use, maintenance and support, and none of the income and payments shall vest in the said cestuis que trustent, or either of them, until payments shall have been made to ~~her~~ or to him, as the case may be.

ITEM 12. In the event of a serious illness or a financial emergency affecting my wife or any of my children, I herewith direct and authorize my Trustee to pay, in [fol. 14] addition to other payments hereinbefore provided

for, to my wife, or to my children, as the case may be, an amount not exceeding Fifteen Hundred Dollars ($1500.00), the said amount to be determined by my Trustee, as in its discretion the same may be necessary, during such illness or financial difficulty. The said payments to any child or children to be considered as an advancement and to be deducted from the respective share of said child or children.

ITEM 13. I nominate, constitute and appoint The First National Bank & Trust Co. of Scranton to be Executor and Trustee of this my Last Will and Testament.

ITEM 14. I hereby direct my Executor and Trustee hereinbefore named to engage Alex Marcus, Esq., as its attorney in the administration of my estate, as well as my Trust Estate.

IN WITNESS WHEREOF, I, CLARENCE C. YOUNG, the Testator, have to this my Last Will and Testament set my hand and seal this 8th day of January, 1957.

(s) Clarence C. Young, (Seal)

Signed, sealed, published and declared by the above-named Testator as and for his Last Will and Testament, in the presence of us, who, at his request, in his presence and in the presence of each other, have subscribed our names as witnesses thereto.

Name (s) Frank M. McDonald,
Residence, 803 Connell Building,
Scranton, Pa.

Name (s) Alex Marcus,
Residence, 803 Connell Building,
Scranton, Pa.

[fol. 15]

EXHIBIT B TO COMPLAINT

U. S. Treasury Department Internal Revenue Service

CLAIM

To be filed with the District Director where assessment was made or tax paid.

District Director's Stamp (Date received)

RECEIVER

24 Jul. 9, 1962

Dis. Dir. Int. Rev.

Scranton, Teller #1

Form 843

(Rev. Mar. 1960)

The District Director will indicate in the block below the kind of claim filed and fill in where required.

☒ Refund of Taxes Illegally, Erroneously, or Excessively Collected.

☐ Refund of Amount Paid for Stamps Unused, or Used in Error or Excess.

☐ Abatement of Tax Assessed (not applicable to estate, gift, or income taxes).

Please Type or Print Plainly

Name of taxpayer or purchaser of stamps: Estate of Clarence C. Young, Northeastern Pennsylvania National Bank and Trust Company, Executor.

[fol. 16] Number and street: P. O. Box No. 831.

City, town, postal zone, State: Scranton, Penna.

Fill in applicable items—Attach letter size sheets if space is not sufficient.

1. Social security number:

2. If an employer, enter employer identification number:

3. District in which return if any was filed: Scranton, Penna.

4. Name and address shown on return if different from above:

5. Period—if for tax reported on annual basis, prepare separate form for each taxable year: Date of death, May 3, 1958.

6. Kind of tax: Estate Tax.

7. Amount of assessment: $14,966.23.

Dates of payment: July 9, 1962.

8. Date stamps were purchased from Government:

9. Amount to be refunded: $14,966.23.

10. Amount to be abated (not applicable to income, estate, or gift taxes):

11. The claimant believes that this claim should be allowed for the following reasons:

> The marital deduction under Section 2056 of the 1954 Internal Revenue Code as amended should be [fol. 17] allowed in full pursuant to the Estate of Gelb v. Commissioner, 298 F. 2d 544 (1962).

I declare under the penalties of perjury that this claim (including any accompanying schedules and statements) has been examined by me and to the best of my knowledge and belief is true and correct.

Signed ....

Dated ...., 19........

Instructions

1. The claim must set forth in detail each ground upon which it is made and facts sufficient to apprise the Commissioner of the exact basis thereof.

2. If a joint income tax return was filed for the year for which this claim is filed, enter social security and employer identification number, if any, of both husband and wife and each must sign this claim even though only one had income.

3. Whenever it is necessary to have the claim executed by an agent on behalf of the taxpayer, an authenticated copy of the document specifically authorizing such agent to sign the claim on behalf of the taxpayer shall accompany the claim.

4. If a return is filed by an individual and a refund claim is thereafter filed by a legal representative of the deceased certified copies of the letters testamentary, letters of administration, or other similar evidence must be annexed to the claim, to show the authority of the executor, administrator, or other fiduciary by whom the claim is filed. If an executor, administrator, guardian, trustee, [fol. 18] receiver, or other fiduciary files a return and thereafter refund claim is filed by the same fiduciary, documentary evidence to establish the legal authority of the fiduciary need not accompany the claim, provided a statement is made on the claim showing that the return was filed by the fiduciary and that the latter is still acting.

5. Where the taxpayer is a corporation, the claim will be signed with the corporate name, followed by the signature and title of the officer having authority to sign for the corporation.

6. If claim is for excess social security (F.I.C.A.) tax withheld as a result of having had more than one employee, include the names and addresses of your employers, and the amount of wages received and taxes withheld by each

as part of your explanation in item 11. Do not claim tax withheld if you have claimed the excess withholding on your individual income tax return.

[fol. 19]

IN THE UNITED STATES DISTRICT COURT

ANSWER—Filed March 25, 1963

The defendant, the United States of America, by and through its attorney, Bernard J. Brown, United States Attorney in and for the Middle District of Pennsylvania, for its answer, admits, denies and alleges as follows:

1. Admits the allegations contained in paragraph 1 of the complaint.

2. Admits the allegations contained in paragraph 2 of the complaint, except denies that any taxes or penalties were erroneously and illegally assessed and collected from the plaintiff.

3. Admits that the jurisdiction of this court, if any, is conferred by the provisions of Title 28, U.S.C. Section 1346(a) (1).

4. Denies the allegations contained in paragraph 4 of the complaint, and avers instead that the plaintiffs are claiming to recover $17,574.45 in taxes and interest assessed and collected from the plaintiffs under the provisions of the Internal Revenue Code of 1954.

5. Denies the allegations contained in paragraph 5 of the complaint, and avers instead that the deficiency of $14,966.23 and interest of $2,608.22 resulted from a reduction of the marital deduction.

[fol. 20] 6. Denies the allegations contained in paragraph 6 of the complaint.

7. Denies the allegations contained in paragraph 7 of the complaint.

8. Admits the allegations contained in paragraph 8 of the complaint, and further admits that the attached Exhibit B is a true and correct copy of the claim for refund except that it lacks the signature and date, but denies each and every allegation contained in the attached Exhibit B unless specifically admitted herein.

9. Admits the allegations contained in paragraph 9 of the complaint, except avers that the notice of rejection is dated September 21, 1962.

10. Admits the allegations contained in paragraph 10 of the complaint, except denies that any assessment, penalties, taxes or interest were overpaid.

11. Denies the allegations contained in paragraph 11 of the complaint.

Wherefore, defendant prays for dismissal of plaintiffs' complaint, judgment in its favor, the costs of this action, and any other relief the Court may deem just and proper.

[fol. 21]

IN THE UNITED STATES DISTRICT COURT

MOTION FOR SUMMARY JUDGMENT—Filed November 7, 1963

The defendant pursuant to Rule 56(b) of the Federal Rules of Civil Procedure, and based upon the pleadings and affidavit annexed hereto moves that the Court enter summary judgment in favor of the defendant for the following reasons:

1. There is no genuine issue of fact.

2. The bequest of $300 per month to the surviving spouse does not qualify as a specific portion pursuant to Section 20.2056(b)-5(c) of the Estate Tax Regulations.

3. The surviving spouse is not entitled to all of the income for life from the amount sought to be deducted.

Bernard J. Brown, United States Attorney.

[fol. 22]

IN THE UNITED STATES DISTRICT COURT

MEMORANDUM—September 30, 1964

This case is before the Court on motions for summary judgment by both plaintiff, Northeastern Pennsylvania National Bank & Trust Company, Executor under the Will of Clarence C. Young, and defendant, United States of America. The pivotal issue centers around plaintiff's entitlement to claim a marital deduction as a result of a testamentary trust.

In the instant case, Clarence C. Young, the decedent, died testate on May 3, 1958, survived by his wife and four children. In the Will, plaintiff, Northeastern Pennsylvania National Bank & Trust Company, was named Executor and Trustee of the estate. Item 6 of the decedent's last Will and Testament provided as follows:

"Item 6. I give, devise and bequeath one-half (½) of all the rest, residue and remainder of my estate, whatsoever and wheresoever the same may be, both real and personal, to which I may be entitled, or which I may have power to dispose of at the time of my death, unto my Trustee hereinafter named and designated, to have and to hold the same in trust, nevertheless, as hereinafter provided.

(a) I direct my Trustee to pay out of the said income and corpus of the said estate unto my wife Beatrice O. Young, the sum of Three Hundred Dollars ($300.00) per month for and during the period until [fol. 23] my youngest child reaches the age of eighteen years, and thereafter I direct my Trustee to pay to my wife, Beatrice O. Young, the sum of Three Hundred Fifty Dollars ($350.00) per month for and during the rest of her natural life.

(b) If my wife survives me, she will have the power, exercisable by Will, to appoint to her estate or to others, any or all of the principal remaining at the

time of her death. If my wife fails to appoint the entire principal to her estate or to others as above mentioned, then upon her death (or if she predeceases me, then upon my death) any principal remaining at that time shall be paid over to my children on the same terms and conditions as under Item 7 of this my Will."

The value of the testamentary residuary trust passing under Item 6 of his Will was $69,245.85, which was listed on the estate tax return by plaintiff as qualifying for the marital deduction pursuant to Section 2056 of the Internal Revenue Code of 1954. The value of the testamentary residuary trust and the property passing outside of the Will to the surviving spouse equalled $110,496.87. The plaintiff claimed a marital deduction in the amount of $99,874.98, constituting one-half of the adjusted gross estate as shown on the return. During the examination, the parties agreed to inclusion of Five Hundred ($500.00) Dollars as the value of household and personal effects specifically devised to the surviving spouse. Subsequently, the government eliminated the full value of the testamentary residuary trust from the marital deduction and thus decreased the amount of the allowable marital deduction to $41,751.02. [fol. 24] The government contends that plaintiff (a) does not qualify for the marital deduction because the surviving spouse is not entitled to all of the income from the entire interest[1] and (b) cannot fit within the definition of a specific

[1] Section 2056(b)-5, Internal Revenue Code of 1954, 26 U.S.C., Sec. 2056

"(5) *Life estate with power of appointment in surviving spouse.*—In the case of an interest in property passing from the decedent, if his surviving spouse is entitled for life to all the income from the entire interest, or all the income from a specific portion thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the interest, or such specific portion, to any person other than the surviving spouse . . ."

portion because Section 20.2056(b)-5 of the Treasury Regulations on Estate Tax requires that in order to qualify as a specific portion, the surviving spouse's rights in income must be a fractional or percentile share and not a fixed amount as is present in this case.[2] Plaintiff disputes de-[fol. 25] fendant's reasons, asserting that the Trust provision establishing a set monthly payment to the surviving spouse did not prevent the property from qualifying as passing to her as she alone received the income payments and she was given the sole right at her death to appoint the then principal under a general power of appointment and, further, assuming that the monthly payments to the surviving spouse do not constitute all the net income of the testamentary residuary trust, the plaintiff should, nevertheless, be entitled to take as a marital deduction the value of the specific portion to which the surviving spouse is entitled, as may be computed actuarially.

The marital deduction was first introduced into the estate tax law as Section 361 of The Revenue Act of 1948, 62 Stat.

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[2] Treasury Regulations on Estate Tax (1954 Code). Sec. 20.2056(b)-5. Marital Deduction; Life Estate with Power of Appointment in Surviving Spouse.

"(c) *Definition of 'specific portion.'* A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse in income and as to the power constitute a fractional or percentile share of a property interest so that such interest or share in the surviving spouse reflects its proportionate share of the increment or decline in the whole of the property interest to which the income rights and the power relate. Thus, if the right of the spouse to income and the power extend to one-half or a specified percentage of the property, or the equivalent, the interest is considered as a specific portion. On the other hand, if the annual income of the spouse is limited to a specific sum, or if she has a power to appoint only a specific sum out of a larger fund, the interest is not a deductible interest. Even though the rights in the surviving spouse may not be expressed in terms of a definite fraction or percentage, a deduction may be allowable if it is shown that the effect of local law is to give the spouse rights which are identical to those she would have acquired if the size of the share had been expressed in terms of a definite fraction or percentage . . ."

110, which amended Section 812(e) of the Internal Revenue Code of 1939. The legislative history of the marital deduction and its revelation of Congressional intent was reviewed by Mr. Justice Goldberg in United States v. Stapf, 375 U.S. 118 (1963), as follows:

> "Our conclusion concerning the congressionally intended result under §812(e) (1) accords with the general purpose of Congress in creating the marital deduction. The 1948 tax amendments were intended to equalize the effect of the estate taxes in community [fol. 26] property and common-law jurisdictions. Under a community property system, such as that in Texas, the spouse receives outright ownership of one-half of the community property and only the other one-half is included in the decedent's estate. To equalize the incidence of progressively scaled estate taxes and to adhere to the patterns of state law, the marital deduction permits a deceased spouse, subject to certain requirements, to transfer free of taxes one-half of the non-community property to the surviving spouse. Although applicable to separately held property in a community property state, the primary thrust of this is to extend to taxpayers in common-law States the advantages of 'estate splitting' otherwise available only in community property States. The purpose, however, is only to permit a married couple's property to be taxed in two stages and not to allow a tax-exempt transfer of wealth into succeeding generations. Thus the marital deduction is generally restricted to the transfer of property interests that will be includible in the surviving spouse's gross estate."

The Act of 1948 also provided that an interest in property passing from the decedent in trust under which the surviving spouse is entitled to all of the income for life, payable at least annually, with power in the surviving spouse to appoint the entire trust corpus, would qualify for the deduction. The Act provided further that certain

interests passing to the surviving spouse which would "terminate" upon a lapse of time or the occurrence or non-occurrence of an event or contingency would not qualify for the deduction. However, the legislation failed to provide for the situation in which the surviving spouse received an interest not in trust or received less than all of [fol. 27] the trust income or the power to appoint less than all of the trust property. To remedy this situation, Section 2056(b)-5 of the Internal Revenue Code of 1954 (see footnote 1) was enacted and provides, in part, that a life estate with power of appointment can qualify for the marital deduction to the extent that the surviving spouse is entitled for life to all of the income from a specific portion thereof with power in the surviving spouse to appoint such specific portion. While the Code itself provides no definition of the term "specific portion", Section 20.2056(b)-5(c) of the Treasury Regulations on Estate Tax (see footnote 2) defines a specific portion as a fractional or percentile share of a property interest. The government asserts that such a definition is consistent with the example of a specific portion found in the committee reports to the 1954 Code.[3] Accordingly, the government concludes that plaintiff is not entitled to claim a marital deduction either (a) as to the

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[3] The Congressional reports state (H. Rep. No. 1337, 83d Cong., 2d Sess., pp. 92, A319 (3 U.S.C. Cong. & Adm. News (1954) 4017, 4119, 4462; S. Rep. No. 1622, 83d Cong., 2d Sess., pp. 125, 475 (3 U.S.C. Cong. & Adm. News (1954) 4621, 4759, 5119):

> The bill makes it clear that property in a legal life estate as well as property in trust qualifies for the marital deduction and that a right to income plus a general power of appointment over only an undivided part of the property will qualify that part of the property for the marital deduction . . .
>
> . . .
>
> For example, if the decedent in his will provided for the creation of a trust under the terms of which the income from one-half of the trust property is payable to his surviving spouse with uncontrolled power in the spouse to appoint such one-half of the trust property by will, such interest will qualify as an exemption from the terminable interest rule.

[fol. 28] value of the entire corpus under the testamentary residuary trust, inasmuch as the surviving spouse is not entitled to all of the income during her life, or (b) as to the alleged specific portion to which the surviving spouse may be entitled, as may be computed actuarially, because the surviving spouse is to receive a fixed amount of income per month and not a fractional or percentile share of income.[4]

As to argument (a), defendant contends that the Committee Reports accompanying the Revenue Act of 1948 make it clear that a trust will not qualify for the marital deduction if the income is required to be accumulated or may, in the discretion of the trustee, be accumulated.[5] In essence, the language from the Committee Reports was incorporated into Section 20.2056(b)-5 (f) (7) of the Treasury Regulations on Estate Tax. Notwithstanding the fact that the corpus has been unable up to this time to produce income of $300 per month, it would appear that plaintiff is not entitled to take as a marital deduction the value of the property passing to the decedent's surviving spouse under the testamentary residuary trust. Under the terms [fol. 29] of the decedent's Will, income from the trust could have exceeded $300 per month and the surplus would then be required to be accumulated. This would run contrary to Congressional intent as expressed in the Committee Reports and could have denied the surviving spouse the

[4] Neither side challenges the fact that by utilizing United States Life Table 38, with interest at 3½ per cent, the present worth of the right to receive $300 per month for the life of a person aged forty-two, which was the surviving spouse's age at the time of decedent's death, is $300 x 12 x 17.3911 x 1.0159 (factor for monthly payments) or $63,663.43. Of course, the government contests the right of the plaintiff to utilize any actuarial computations.

[5] See S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., p. 17 (1948-1 Cum. Bull. 285, 342-343): "(3) The surviving spouse must be entitled to the income from the corpus of the trust annually, or at more frequent intervals. This requirement disqualifies any trust the income of which is required to be accumulated or may, in the discretion of the trustee, be accumulated."

full enjoyment as virtual owner of the property. By way of example, a testator could create a testamentary trust with a corpus of One Million Dollars and provide income of $100 per month to the surviving spouse with no income entitlement to anyone else. Consequently, no one else would share in the income, but there would necessarily have to be an accumulation which would most certainly deny the surviving spouse of her full enjoyment as virtual owner of the property. Hence the need for a determination as to what the terms of the trust instrument could produce and not what ultimately occurs. "We cannot wait like 'Monday morning quarterbacks,' to see what actually happened but must concern ourselves to what *could* have happened . . . " Bookwalter v. Lamar, 323 F. 2d 664 (8th Cir. 1963). It must be remembered that a taxpayer seeking the benefit of a deduction must show that every condition has been fully satisfied which Congress has seen fit to impose. Deputy v. DuPont, 308 U.S. 488; New Colonial Co. v. Helvering, 292 U.S. 435. Congress has made it a condition to marital deduction entitlement for the entire corpus, that the surviving spouse be entitled to all of the income from the trust. The terms of the trust instrument provide for the payment of $300 per month, which does not require that the surviving spouse receive all of the income annually. Consequently, plaintiff is not entitled to take as a marital deduction the value of the property passing to the decedent's surviving spouse under the testamentary residuary trust.

[fol. 30] As to plaintiff's alternative position, i.e., that plaintiff should be entitled to take as a marital deduction the value of the specific portion to which the surviving spouse is entitled, as may be computed actuarially, a different result may be warranted. In other words, plaintiff asserts that the surviving spouse is absolutely entitled to $300 per month and if this amount is construed to represent income from corpus, then by actuarial computation, the amount of corpus that would yield this income can be

ascertained and should be treated as qualifying as a specific portion for marital deduction purposes.

The government makes much of the argument that Section 20.2056(b)-5(c) of the Estate Tax Regulations is consistent with the statute and must be followed. This regulation provides that in order to be treated as a specific portion, the rights of the surviving spouse in income and as to the power must constitute a fractional or percentile share and if the annual income of the spouse is limited to a specific sum, then the interest is not a deductible interest. The underlying reason for this regulation, according to the government, is that the interest or share in the surviving spouse must "reflect its proportionate share of the increment or decline in the whole of the property interest to which the income rights and the power relate." That is, that both the government and the surviving spouse share equally in the risk of the property decreasing in value (and thus the ultimate tax decreasing) and of the property increasing in value (and thus the ultimate tax increasing). This argument was rejected by the Court of Appeals for the Second Circuit in Gelb v. Commissioner of Internal Revenue, 298 F. 2d 544 (1962). In that case, the widow, under the re- [fol. 31] siduary trust was entitled to at least $10,000.00 a year; principal to be invaded if necessary. The widow was given the power to appoint the principal by will. The trustees, the widow and her son, had the discretion to advance from the corpus, an amount not in excess of $5,000.00 a year for the support and education of the youngest daughter. The Court held that the entire trust property did not qualify for the marital deduction, but that the capitalized vaule of $5,000.00 per annum[6] could be carved out of the corpus and that the corpus, as diminished, would qualify for the marital deduction.

"The Commissioner does not argue that the divergency between the extent of Rose's (the widow) right

[6] This would be accomplished by multiplying the present value of $5,000.00 by the joint life expectancy of the widow (Rose) and the youngest daughter (Claire).

to income and her power to appoint prevents her interest from constituting a 'specific portion' . . . The Commissioner's argument is rather that here even the smaller portion, that over which the right to appoint corpus extends, does not qualify because it is not the 'fractional or percentile share' demanded by the Regulations . . ."

". . . True, when the power is to draw a specific dollar amount the spouse bears no risk of change in the value of the corpus, unless, indeed, it shrinks below the dollar figure; and when the power is over all the corpus except a named dollar amount, the spouse is saddled with a disproportionate risk. However, Congress spoke of a 'specific portion' not of a 'fractional or percentile share,' and nowhere indicated any policy that deductibility of a 'specific portion' should be gov- [fol. 32] erned by the possibility that the spouse's portion will change in value relatively more or less than the clearly nonqualifying part. Neither has the Commissioner given us any reason why this should be so. A basic purpose of the marital deduction was to reduce the discrimination against taxpayers not in community property states, S. Rep. No. 1013, 80th Cong., 2nd Sess., in 1948-1 C. B. at pp. 305-306; see Commissioner v. Estate of Ellis, (58-1 USTC 11, 746) 252 F. 2d 109, 112 (3 Cir. 1958). The liberalization in the provision as to trusts, made in the 1954 Code and applied to earlier years by the Technical Amendments Act, was evidently designated to permit certain normal testamentary dispositions without the total forfeiture of the deduction that the 1939 Code had occasioned in some instances. That Congress gave a fractional interest as an example of a 'specific portion' does not warrant a construction that Congress did not mean to include other instances fairly within the language and the underlying policy. We disapprove Regulations 105, §81.47 a(c) (3) (1954 Code—Regs. §20.2056 (b)-

> 5(c)) insofar as it would limit a 'specific portion' to 'a fractional or percentile share.'"
>
> "However, the taxpayers here encounter an added difficulty. Rose's qualifying power was not over the entire corpus less a sum described in dollars, but over all less a sum which can at best be estimated by actuarial calculations. It is surely arguable that in the latter case the power is not exercisable over a 'specific portion' even though in the former it is—the joint lives of Rose and Claire might differ substantially from their actuarial expectancy. Yet the use of [fol. 33] actuarial tables for dealing with estate tax problems has been so widespread and of such long standing that we cannot assume Congress would have balked at it here; the United States is in business with enough different taxpayers so that the law of averages has ample opportunity to work."

It is true that in Gelb the surviving spouse was entitled to all the income, although her power of appointment over the corpus was reduced by the amount needed for her daughter's education. However, the principle enunciated in Gelb has similar application here where the surviving spouse's entitlement to income was confined to $300, although she retained full power of appointment over the entire corpus. The actuarial computation mentioned and approved in Gelb can be just as feasibly applied here. While I recognize that administrative interpretation is entitled to great weight, I agree with the reasoning in Gelb that the Congressional ". . . example of a 'specific portion' does not warrant a construction that Congress did not mean to include other instances fairly within the language and the underlying policy."

Applying the actuarial computation described in footnote 4, and adding this sum of $63,663.43 to the $41,751.02 marital deduction heretofore allowed by defendant, a total of $105,414.45 is reached, which exceeds the $99,874.98 marital deduction claimed by plaintiff in the estate tax

return. Consequently, plaintiff is entitled to the full marital deduction of $99,874.98 and judgment will be entered for $17,574.45, representing the tax unlawfully collected [fol. 34] by defendant when the specific portion of the testamentary residuary trust was erroneously disallowed.

William J. Nealon, United States District Judge.

September 30, 1964.

In the United States District Court

Order Granting Plaintiff's Motion for Summary Judgment—September 30, 1964

Now, this 30th day of September, 1964, in accordance with the Memorandum this day filed, it is hereby Ordered and Decreed that plaintiff's motion for summary judgment is granted and judgment is entered in favor of the plaintiff and against the defendant in the amount of $17,574.45 with interest, as provided by law. Defendant's motion for summary judgment is denied.

William J. Nealon, United States District Judge.

[fol. 35]

In the United States District Court

Notice of Appeal—Filed November 27, 1964

F.R.C.P. Rule 73(a), (b)

Notice is hereby given that the United States of America, Defendant above named, hereby appeals to the United States Court of Appeals for the Third Circuit from the final judgment entered in this action on September 30, 1964.

Bernard J. Brown, United States Attorney, Attorney for Appellant United States of America.

Dated: November 27, 1964.

[fol. 35a]

IN THE UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 15,249

NORTHEASTERN PENNSYLVANIA NATIONAL BANK & TRUST COMPANY, Executor Under the Will of CLARENCE C. YOUNG

v.

UNITED STATES OF AMERICA, Appellant.

Appellee's Appendix

[fol. 36]

Internal Revenue Code of 1954

Internal Revenue Code of 1954, Section 2056. (a) Allowance of Marital Deduction.—For the purposes of the tax imposed by Section 2001, the value of the taxable estate shall, except as limited by subsections (b), (c), (d), be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

(b) Limitation in the Case of Life Estate or Other Terminable Interest.—

(1) General Rule.—Where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate

or fail, no deduction shall be allowed under this section with respect to such interest—

(A) if an interest in such property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to any person other than such surviving spouse (or the estate of such spouse); and

(B) if by reason of such passing such person (or his heirs or assigns) may possess or enjoy any part of such property, after such termination or failure [fol. 37] of the interest so passing to the surviving spouse; and no deduction shall be allowed with respect to such interest (even if such deduction is not disallowed under subparagraphs (A) and (B)).—

(C) if such interest is to be acquired for the surviving spouse, pursuant to directions of the decedent, by his executor or by the trustee of a trust. For purposes of this paragraph, an interest shall not be considered as an interest which will terminate or fail merely because it is the ownership of a bond, note, or similar contractual obligation, the discharge of which would not have the effect of an annuity for life or for a term.

* * * * * * *

(5) Life Estate With Power of Appointment in Surviving Spouse.—In the case of an interest in property passing from the decedent, if his surviving spouse is entitled for life to all the income from the entire interest, or all the income from a specific portion thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of

others), and with no power in any other person to appoint any part of the interest, or such specific portion, to any person other than the surviving spouse—

(A) the interest or such portion thereof so passing shall, for purposes of subsection (a), be considered as passing to the surviving spouse, and

[fol. 38] (B) no part of the interest so passing shall, for purposes of paragraph (1)(A), be considered as passing to any person other than the surviving spouse. This paragraph shall apply only if such power in the surviving spouse to appoint the entire interest, or such specific portion thereof, whether exercisable by will or during life, is exercisable by such spouse alone and in all events.

* * * * * * *

(26 U.S.C. 1958 ed., Sect. 2056)

Treasury Regulations on Estate Tax
(1954 Code)

§20.2056(b)-1 Marital Deduction; Limitation in Case of Life Estate or Other "Terminable Interest"—

(a) In General. Section 2056(b) provides that no marital deduction is allowed with respect to certain property interests, referred to generally as "terminable interests," passing from a decedent to his surviving spouse....

(b) "Terminable Interests." A "terminable interest" in property is an interest which will terminate or fail on the lapse of time or on the occurrence or the failure to occur of some contingency. Life estates, terms for years, annuities, patents, and copyrights are therefore terminable interests.

(c) Nondeductible Terminable Interests. (1) A property interest which constitutes a terminable in-

[fol. 39] terest, as defined in paragraph (b) of this section, is nondeductible if—

(i) Another interest in the same property passed from the decedent to some other person for less than an adequate and full consideration in money or money's worth, and

(ii) By reason of its passing, the other person or his heirs or assigns may possess or enjoy any part of the property after the termination or failure of the spouse's interest.

* * * * * * *

§20.2056(b)-4 Marital Deduction; Valuation of Interest Passing to Surviving Spouse—

(d) Remainder Interests. If the income from property is made payable to another individual for life, or for a term of years, with remainder absolutely to the surviving spouse or to her estate, the marital deduction is based upon the present value of the remainder. The present value of the remainder is to be determined in accordance with the rules stated in §20.2031-7.

* * * * * * *

§20.2056(b)-5 Marital Deduction; Life Estate With Power of Appointment in Surviving Spouse—

(a) In General. Section 2056(b)(5) provides that if an interest in property passes from the decedent to his surviving spouse (whether or not in trust) and the spouse is entitled for life to all the income from the [fol. 40] entire interest or all the income from a specific portion of the entire interest, with a power in her to appoint the entire interest or the specific portion, the interest which passes to her is a deductible interest, to the extent that it satisfies all five of the conditions set forth below (see paragraph (b) of this section if one or more of the conditions is satisfied as to only a portion of the interest):

(1) The surviving spouse must be entitled for life to all of the income from the entire interest or a specific portion of the entire interest, or to a specific portion of all the income from the entire interest.

(2) The income payable to the surviving spouse must be payable annually or at more frequent intervals.

(3) The surviving spouse must have the power to appoint the entire interest or the specific portion to either herself or her estate.

(4) The power in the surviving spouse must be exercisable by her alone and (whether exercisable by will or during life) must be exercisable in all events.

(5) The entire interest or the specific portion must not be subject to a power in any other person to appoint any part to any person other than the surviving spouse.

(b) Specific Portion; Deductible Amount. If either the right to income or the power of appointment passing to the surviving spouse pertains only to a specific portion of a property interest passing from the decedent, the marital deduction is allowed only to the [fol. 41] extent that the rights in the surviving spouse meet all five conditions described in paragraph (a) of this section. While the rights over the income and the power must coexist as to the same interest in property, it is not necessary that the rights over the income or the power as to such interest be in the same proportion. However, if the rights over income meeting the required conditions set forth in paragraph (a)(1) and (2) of this section extend over a smaller share of the property interest than the share with respect to which the power of appointment requirements set forth in paragraph (a)(3) through (5) of this section are satisfied, the deductible interest is limited to the smaller share. Correspondingly, if a power of appointment

~~meeting all~~ the requirements extends to a smaller portion of the property interest than the portion over which the income rights pertain, the deductible interest cannot exceed the value of the portion to which such power of appointment applies. Thus, if the decedent leaves to his surviving spouse the right to receive annually all of the income from a particular property interest and a power of appointment meeting the specifications prescribed in paragraph (a)(3) through (5) of this section as to only one-half of the property interest, then only one-half of the property interest is treated as a deductible interest. Correspondingly, if the income interest of the spouse satisfying the requirements extends to only one-fourth of the property interest and a testamentary power of appointment satisfying the requirements extends to all of the property interest, then only one-fourth of the interest in the spouse qualifies as a deductible interest. Further, if the surviving spouse has no right to income from a [fol. 42] specific portion of a property interest but a testamentary power of appointment which meets the necessary conditions over the entire interest, then none of the interest qualifies for the deduction. In addition, if, from the time of the decedent's death, the surviving spouse has a power of appointment meeting all of the required conditions over three-fourths of the entire property interest and the prescribed income rights over the entire interest, but with a power in another person to appoint one-half of the entire interest, the value of the interest in the surviving spouse over only one-half of the property interest will qualify as a deductible interest.

(c) Definition of "Specific Portion". A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse in income and as to the power constitute a fractional or percentile share of a property interest so

that such interest or share in the surviving spouse reflects its proportionate share of the increment or decline in the whole of the property interest to which the income rights and the power relate. Thus, if the right of the spouse to income and the power extend to one-half or a specified percentage of the property, or the equivalent, the interest is considered as a specific portion. On the other hand, if the annual income of the spouse is limited to a specific sum, or if she has a power to appoint only a specific sum out of a larger fund, the interest is not a deductible interest. Even though the rights in the surviving spouse may not be expressed in terms of a definite fraction or percentage, [fol. 43] a deduction may be allowable if it is shown that the effect of local law is to give the spouse rights which are identical to those she would have acquired if the size of the share had been expressed in terms of a definite fraction or percentage.

(e) Application of Local Law. In determining whether or not the conditions set forth in paragraph (a)(1) through (5) of this section are satisfied by the instrument of transfer, regard is to be had to the applicable provisions of the law of the jurisdiction under which the interest passes and, if the transfer is in trust, the applicable provisions of the law governing the administration of the trust.

(f) Right to Income. (1) If an interest is transferred in trust, the surviving spouse is "entitled for life to all of the income from the entire interest or a specific portion of the entire interest," for the purpose of the condition set forth in paragraph (a)(1) of this section, if the effect of the trust is to give her substantially that degree of beneficial enjoyment of the trust property during her life which the principles of the law of trusts accord to a person who is unqualifiedly designated as the life beneficiary of a trust. Such degree of enjoyment is given only if it was the

decedent's intention, as manifested by the terms of the trust instrument and the surrounding circumstances, that the trust should produce for the surviving spouse during her life such an income, or that the spouse should have such use of the trust property as is consistent with the value of the trust corpus and with its preservation. The designation of the spouse as sole income beneficiary for life of the entire inter-[fol. 44] est or a specific portion of the entire interest will be sufficient to qualify the trust unless the terms of the trust and the surrounding circumstances considered as a whole evidence an intention to deprive the spouse of the requisite degree of enjoyment. In determining whether a trust evidences that intention, the treatment required or permitted with respect to individual items must be considered in relation to the entire system provided for the administration of the trust.

* * * * * * *

(26 C.F.R. Sec. 20.2056(b)-1, 4, 5)

Last Will and Testament of Clarence C. Young

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* * * * * * *

Item 6. I give, devise and bequeath one-half ($\frac{1}{2}$) of all the rest, residue and remainder of my estate, whatsoever and wheresoever the same may be, both real and personal, to which I may be entitled, or which I may have the power to dispose of at the time of my death, unto my Trustee hereinafter named and designated, to have and to hold the same in trust, nevertheless, as hereinafter provided.

(a) I direct that my Trustee pay out of the said income and corpus of the said estate unto my wife, Beatrice O. Young, the sum of Three Hundred dollars ($300.00) per month for and during the period

until my youngest child reaches the age of eighteen years, and thereafter I direct my Trustee to pay to [fol. 45] my wife, Beatrice O. Young, the sum of Three Hundred Fifty dollars ($350.00) per month for and during the rest of her natural life.

(b) If my wife survives me, she shall have the power, exercisable by Will, to appoint to her estate, or to others, any or all of the principal remaining at the time of her death. If my wife fails to appoint the entire principal to her estate or to others as above authorized, then upon her death (or if she predeceases me, then upon my death) any principal remaining at that time shall be paid over to my children on the same terms and conditions as under Item 7 of this my Will.

[fol. 46]

STIPULATION AND ORDERS EXTENDING THE TIME FOR FILING APPELLANT'S BRIEF AND APPENDIX

[fol. 48]

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 15249

NORTHEASTERN PENNSYLVANIA NATIONAL BANK & TRUST COMPANY, Executor Under the Will of CLARENCE C. YOUNG,

vs.

UNITED STATES OF AMERICA, Appellant.

(D.C. No. 7993)

Present: Kalodner, Chief Judge, and McLaughlin, Staley Hastie, Forman, Ganey, Smith and Freedman, Circuit Judges.

ORDER SETTING CASE DOWN FOR REHEARING BEFORE THE COURT EN BANC—March 2, 1966

It is Ordered that the above entitled case be and it hereby is set down for rehearing before the Court en Banc, the date to be fixed by the Clerk of this Court.

By the Court, J. Cullen Ganey, Circuit Judge.

Dated: March 2, 1966.

[fol. 49]

United States Court of Appeals

For the Third Circuit

No. 15249

Northeastern Pennsylvania National Bank & Trust Company, Executor Under the Will of Clarence C. Young,

v.

United States of America, Appellant.

Appeal From the United States District Court for the Middle District of Pennsylvania

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Argued October 18, 1965

Reargued June 9, 1966

Before Staley, Chief Judge, and McLaughlin, Kalodner, Hastie, Forman, Ganey, Smith and Freedman, Circuit Judges.

Opinion of the Court—Filed July 19, 1966

By Forman, *Circuit Judge.*

This is an appeal by the defendant, United States of America (hereinafter appellant) from a summary judgment entered by the United States District Court for the Middle District of Pennsylvania on the motion of plaintiff, Northeastern Pennsylvania Bank and Trust Company, [fol. 50] Executor under the will of Clarence C. Young (hereinafter appellee), in the amount of $17,574.45 with interest, and from the denial of appellant's motion for summary judgment. Appellee's suit alleged an improper rejection of a claimed marital deduction.

Decedent died testate on May 3, 1958, survived by his wife and four children. Paragraph 6 of decedent's will[1] provided for the bequest of one-half of the residue of the estate to appellee who was directed to pay out of income, and corpus if necessary, the sum of $300 per month to decedent's wife until his youngest child reached eighteen years of age, after which appellee was directed to pay decedent's wife $350 per month for the rest of her life. Paragraph 6 also provided that if decedent's wife survived him, she would have the power, exercisable by will, to appoint to her estate, or to others, any or all of the principal of the trust remaining at the time of her death. Paragraph 11[2] recited that such stipends were in no event to be liable

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[1] "ITEM 6. I give, devise and bequeath one-half (½) of all the rest, residue and remainder of my estate, whatsoever and wheresoever the same may be, both real and personal, to which I may be entitled, or which I may have power to dispose of at the time of my death, unto my Trustee hereinafter named and designated, to have and to hold the same in trust, nevertheless, as hereinafter provided.

"(a) I direct my Trustee to pay out of the said income and corpus of the said estate unto my wife, Beatrice O. Young, the sum of Three Hundred Dollars ($300.00) per month for and during the period until my youngest child reaches the age of eighteen years, and thereafter I direct my Trustee to pay to my wife, Beatrice O. Young, the sum of Three Hundred Fifty Dollars ($350.00) per month for and during the rest of her natural life.

"(b) If my wife survives me, she shall have the power, exercisable by Will, to appoint to her estate, or to others, any or all of the principal remaining at the time of her death. If my wife fails to appoint the entire principal to her estate or to others as above authorized, then upon her death (or if she predeceases me, then upon my death) any principal remaining at that time shall be paid over to my children on the same terms and conditions as under Item 7 of this my Will."

[2] "ITEM 11. The income and payments herein provided for my wife and children and the issue of my children are for their, and each of their, sole and separate use, maintenance and support, and are in no event to be liable for any debts contracted by them or any of them, and are not to be liable to attachment or assignment,

[fol. 51] for any debts contracted by the survivor and were not to be liable to attachment or assignment, but were solely for the use, maintenance and support of the survivor.[3] Paragraph 11 also indicated that income produced from the corpus of the trust which exceeds the monthly allotment is to be accumulated. Paragraph 12[4] of the will granted appellee the power to authorize payments over and above the monthly stipend up to $1500 in the event of a serious illness or financial emergency affecting the surviving spouse. Whether the figure of $1500 is in the aggregate or may be paid in each event is unclear.

Decedent's adjusted gross estate was $199,749.96. Appellee sought to qualify the maximum amount, one-half of that adjusted gross estate, $99,874.98, as a marital deduction in accordance with Sections 2056(c)(1)[5] and 2056(b)(5)[6] of the 1954 Internal Revenue Code. The value of the property passing outside the will, to the decedent's spouse, $41,751.02, was combined on the estate tax return with the full value of the testamentary residuary trust,

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but are solely and exclusively for their and each of their sole and individual use, maintenance and support, and none of the income and payments shall vest in the said cestuis que trustent, or either of them, until payments shall have been made to her or to him, as the case may be."

[3] Whether such limitations are valid has no bearing here as we are only interested in them as they reflect the decedent's intent.

[4] "ITEM 12. In the event of a serious illness or a financial emergency affecting my wife or any of my children, I herewith direct and authorize my Trustee to pay, in addition to other payments hereinbefore provided for, to my wife, or to my children, as the case may be, an amount not exceeding Fifteen Hundred Dollars ($1500.00), the said amount to be determined by my Trustee, as in its discretion the same may be necessary, during such illness or financial difficulty. The said payments to any child or children to be considered as an advancement and to be deducted from the respective share of said child or children."

[5] 26 U.S.C. § 2056(c)(1) (1965).

[6] 26 U.S.C. § 2056(b)(5) (1965).

$69,245.85, to total $110,996.87. That portion of $110,996.87 which constituted one-half of the adjusted gross estate, $99,874.98, was listed, as noted above, as qualifying for the marital deduction. Appellant eliminated the full value of the testamentary residuary trust from the claimed marital deduction and thus decreased the amount of the allowable marital deduction to $41,751.02. The deficiency in estate tax was paid, a claim for refund was disallowed, appellee filed suit for refund, and after motions for [fol. 52] summary judgment were presented by both parties, the District Court ruled in favor of the appellee and granted the refund.[7]

The District Court did not, as proposed by appellee, conclude that the entire value of the trust corpus, $69,245.85, could be considered for the marital deduction. Instead, it applied a Treasury Department actuarial formula to value the present worth of the surviving spouse's monthly stipend. This formula produced a value of $63,663.43. This was added to $41,751.02, the value of the property passed to the surviving spouse outside the will, to total $105,414.45, an amount in excess of one-half of the decedent's adjusted gross estate, $99,874.98, the maximum allowable statutory marital deduction. The District Court thus concluded that appellee was entitled to the full marital deduction of $99,874.98, and judgment was entered for $17,574.45 plus interest, representing the tax found to have been unlawfully collected by appellant.

—I—

As the marital deduction provisions function today, under a trust arrangement such as the one involved herein, the entire corpus of the trust qualifies for inclusion in the estate tax return as part of the marital deduction if each of two prerequisites[8] are met: (1) the surviving spouse is

[7] Northeastern Pennsylvania Nat. B. & T. Co. v. United States, 235 F. Supp. 941 (M.D.Pa. 1964).

[8] There are other contingencies not relevant to the problem at hand.

entitled to all the income produced from the corpus for the remainder of the survivor's life with (2) power in the survivor to appoint the entire corpus remaining at the time of the power's exercise. If the survivor's requisite relationship to the corpus bars the qualification of the entire corpus for the deduction, a part of the trust corpus will qualify for marital deduction status if the survivor is entitled to the income from a "specific portion" of the whole, whether there be a power to appoint the entire [fol. 53] interest remaining at the time of the power's exercise or the power to appoint only a part thereof.[9] Appellant's administrative regulation[10] has defined "specific portion" as a fractional or percentile part of the entire corpus. The practical effect of the marital deduction is to defer taxation of some part of the decedent's estate passing to the surviving spouse until the death of the surviving spouse.

Reviewing the purpose of the marital deduction, Mr. Justice Goldberg speaking for a unanimous court in *United States* v. *Stapf*[11] explained:

> "The 1948 tax amendments were intended to equalize the effect of the estate taxes in community property and common-law jurisdictions.[12] [Footnote omitted.] Under a community property system, such as that in Texas, the spouse receives outright ownership of one-half of the community property and only the other one-

[9] Consistent with this, only a part of the corpus will qualify for marital deduction status if the survivor is entitled to all the income from the corpus for life but may only appoint a "specific portion" of the remainder of the corpus at the time of the power's exercise. Similarly, only a part of the corpus, the smaller of the two specific portions, will qualify for marital deduction status if only a "specfic portion" of the income may go to the survivor for life and if the survivor's power of appointment is limited to a "specific portion" of the remaining corpus at the time of the power's exercise. See 26 C.F.R. § 20.2056(b)-5(b) (1961).

[10] 26 C.F.R. § 20.2056(b)-5(b) (1961).

[11] 375 U.S. 118, 128 (text and n.12) (1963).

half is included in the decedent's estate. To equalize the incidence of progressively scaled estate taxes and to adhere to the patterns of state law, the marital deduction permits a deceased spouse, subject to certain requirements, to transfer free of taxes one-half of the non-community property to the surviving spouse. Although applicable to separately held property in a community property state, the primary thrust of this is to extend to taxpayers in common-law states the advantages of 'estate splitting' otherwise available only in community property States."

[fol. 54] Problems that have arisen in this area have in the main concerned the extent to which the advantages of estate-splitting are to be allowed. Towards clarification of this issue, the above noted interpretive regulation was promulgated. A detailed discussion of the congressional intent behind the passage of the 1948 Revenue Act appears in Senate Report No. 1013, March 16, 1948 [to accompany H.R. 4790]. In that Report, the marital deduction additions to the 1949 Code are characterized as follows:

> "These provisions have the effect of allowing a marital deduction with respect to the value of property transferred in trust or at the direction of the decedent *where the surviving spouse*, by reason of her right to the income and a power of appointment, *is the virtual owner of the property.*" [12]

And, as above detailed, the virtual ownership interest encompasses that existent in a "specific portion" of the trust corpus.

In sum, the propriety of granting a marital deduction in this case must be measured by the purpose of the marital deduction as expressed in *Stapf*, the interpretive regulation

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[12] 2 U.S. Code Cong. and Ad. News, 80th Cong., 2nd Session, p. 1238 (1948) (Emphasis added.)

as promulgated by the Internal Revenue Service, the expression of the congressional intent on the subject, and the decedent's intent in structuring the existent trust arrangement.

—II—

As the survivor has been given in Paragraph 6 the right to appoint the entire corpus, no question arises in this case concerning the "specific portion" of the corpus to which the power extends. The contentions concern solely the relationship between the survivor's monthly stipend and the trust corpus—whether the decedent's trust arrangement placed in his surviving spouse the right to all the income from the corpus, or all the income from a "specific portion" [fol. 55] thereof? The appellee has offered alternative arguments, as it did before the District Court, to justify either the inclusion of the entire $69,245.85 residuary trust in the estate tax return as appropriate for marital deduction status or the inclusion of $63,663.43 in the return as a "specific portion" of the residuary trust thus qualifying for marital deduction status.

The District Court rejected, properly we believe, appellee's contention that the entirety of the trust corpus of $69,245.85 be entitled to marital deduction status. It was pointed out that appellee's position fails for, in deciding whether the survivor is entitled to receive all the income from the trust corpus for life, the determinative factor is what income the trust corpus *could* produce and not what is *now* being produced, or what ultimately *will* be produced. Here, the corpus may be able to produce more than the survivor's monthly stipend. The surplus would have to be accumulated and the survivor would have no right to the *present enjoyment* of the excess income, even though, as argued by appellee, she would have the power to appoint it. Thus, the survivor would not be entitled to the entire income which might come from the corpus, within the intendment of Section 2056(b)(5) of the 1954 Internal Revenue

Act.[13] This very real consideration must also be given appropriate weight in determining whether the survivor is entitled to the income from a "specific portion" of the trust, and what such "specific portion" is.

Was appellee, as found by the District Court, entitled to the inclusion in its tax return of $63,663.43 from the corpus as a "specific portion" thereof—a part in which the surviving spouse had a total income interest? The method [fol. 56] of actuarial computation used by the District Court, along with the efficacy of the use of any actuarial method of computing "specific portion", is of primary concern and requires analysis. It is well to underline the statutory language which must be considered in this respect. Section 2056(b)(5) of the Code makes it clear that "specific portion" is that part of the trust corpus from which the surviving spouse is entitled to "all the income." Thus, unless the actuarial formula used by the District Court succeeds in isolating that part of the trust corpus from which the survivor is entitled to *all* the income for her lifetime, the computation is of no value. The actuarial method on which this case has been turned does not, in our view, isolate that part of the trust corpus from which the surviving spouse is entitled to all the income.

The District Court, in computing the present worth of the survivor's monthly stipend, applied a formula used by the Treasury Department in the "valuation of annuities, life estates, terms for years, remainders and reversions." This may be found in 26 C.F.R. § 20.2031-7 (1961). The formula valued the worth of the monthly stipends by multi-

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[13] It should be noted in passing that it would be unrealistic to conceive of an unlimited income potential from a trust whose trustees, by law, must stay within the bounds of certain guidelines. Such a consideration may play a part in another case at another time. Here, however, appellee does not argue, nor does the record reflect, that the appellee, by law, cannot invest the corpus to produce an income in excess of the monthly stipend. Thus the potentiality of the production of an income in excess of the monthly stipend to the survivor is a real factor which has been, and must be, given its due weight by the courts.

plying together the following factors: \$300 (amount of monthly payment); 12 (number of months in a year); 1.0159 (factor for monthly payments); and 17.3911 (factor for the discount rate of 3½ percent over the period of the widow's life expectancy). The present worth of the \$300 monthly stipend was determined to be \$63,663.43, a "specific portion" of the trust corpus, and thus qualifying for marital deduction status. The District Court thus rejected the Treasury Regulation noted above so far as it required the "specific portion" to be specified in fractional or percentile form.

As an initial matter, we find the formula inappropriate in determining what part of a trust corpus may be considered a "specific portion" for marital deduction purposes. First, the mere fact that the formula is one for valuing an annuity eliminates it as appropriate for determining "specific [fol. 57] portion." The factor 17.3911 in the formula represents the present worth of one dollar invested in an annuity at 3½ percent over the remaining life expectancy of a person forty-two years of age, the age of the surviving spouse at the decedent's death. The formula thus provides a discount value through a process of capitalizing at 3½ percent what was directed to be \$300 monthly payments. If \$63,663.43 is invested at age forty-two, that amount will provide the annuitant the required monthly payments for her entire life. At death the entire fund will have been dissipated. However, the factor of fund dissolution has in no way been contemplated by the decedent. The formula thus intrudes an artificial element into our problem, an element inconsistent with what the District Court in effect conceded to be the income production potential of the corpus when it ruled that appellee was not entitled to a marital deduction for the full value of the trust corpus.

Second, the monthly stipend allotted under the trust arrangement, \$300 initially, is placed into the formula as the amount of *income* which a given fund must produce. However, under the trust arrangement, the trustees have not been directed to invest the corpus so that it will yield

a given monthly income. All that has been directed is that the survivor receive such income, *even if corpus must be invaded* to make up the difference between the income yield of the corpus per month and the stipend allotment. And if the income yield be greater than $300 in a given month, the excess is to be accumulated. Thus, inclusion of the $300 figure in the formula is inappropriate for it equates the monthly stipend with the income yield from the corpus, elements which are in no way interchangeable.

Third, and this has a direct bearing on the point just made, the formula may be characterized as one which attempts to capitalize a given monthly stipend and produce a capital value, $63,663.43, which is to be the "specific portion" for marital deduction purposes. Such a method of computation is improper for we already know what is [fol. 58] the value of the entire trust. Only from that given value of $69,245.85 may any computation of "specific portion", if any be appropriate, proceed. Under the formula used by the District Court, the results that may be reached demonstrate the inappropriateness of a capitalization method which disregards the present value of the trust corpus. Assume for a moment a direction that appellee pay $350 monthly as a stipend to the surviving spouse as of the date of decedent's death. Capitalizing a $350 monthly stipend under the District Court's formula for determining "specific portion", the capital value figure reached is $74,199.80, a sum in excess of the value of the entire trust corpus. As stated above it is conceded that the estate is not entitled to a marital deduction for the sum of the entire trust corpus, because of the potentialities of income production. Yet, under the actuarial formula used to determine "specific portion", the formula accepted by the District Court, at least the entire value of the corpus is to qualify for the deduction as a "specific portion" of the entirety, and theoretically a sum in excess of the entire trust corpus's value will qualify. The incongruity of equating the monthly stipend with the income yield is manifest.

Finally, in determining the "specific portion" of a given trust corpus from which part the survivor has an absolute income right, actuarial computation is inappropriate when the formula uses variable factors other than mere life expectancy. The use of the monthly stipend as the income factor in the formula noted above exemplifies the attempt to make constant that which is variable in this case. The 3½ percent investment factor in the actuarial formula is likewise unreal. As previously indicated, Congress's intent was to give a marital deduction to those interests of a surviving spouse in a common law jurisdiction which were akin to the fee simple interest held by a survivor in a community property state. Such an interest, to qualify as akin to a fee simple interest, must be subject to the rise and fall of the market. An investment constant, such as [fol. 59] 3½ percent in the instant case, though accepted in actuarial formulas, has no place in a problem where the very real income variations turn the issue of the allowance of the marital deduction. Indeed, the use of such a constant is absent from the regulations dealing with the "specific portion" issue, whereas it may be found in the regulations in formulas geared to different problems.

Having attempted to demonstrate the inappropriateness of the formula used by the District Court, the question arises as to whether, under the facts of this case, there does exist a method for isolating a "specific portion" of the trust corpus to qualify for marital deduction status? The term "specific portion" has been appropriately defined in this manner:

> "Presumably, specific portion does not mean anything more than a designation of the amount of the surviving spouse's interest *which makes it feasible to compute the amount of the marital deduction.*" [14]

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[14] Lowndes and Kramer, Federal Estate and Gift Taxes 407 (1956). (Emphasis added.)

Feasible computation of a "specific portion" is the key to marital deduction status.

The Internal Revenue Service in its above noted regulation considers any testamentary trust which describes the relationship between the income to be received by the survivor and the trust corpus in anything but "fractional or percentile" terms as one which expresses a relationship falling outside the susceptibility of computation, and thus one which thwarts a determination of "specific portion" for purposes of the marital deduction. *Gelb* v. *C.I.R.*,[15] heavily relied upon by appellee and the District Court, expressed a view which is contrary to the interpretive regulation. In *Gelb* the surviving spouse was entitled to *all* the income from the trust corpus for her life. As distinguished from the case at hand, the issue in *Gelb* was [fol. 60] whether the survivor had a power of appointment over a "specific portion" of the trust corpus. That problem arose because the trustees in *Gelb* were empowered to invade the corpus, in their discretion, to the extent of $5,000 per year for the support, education and maintenance of the decedent's minor daughter. The Government argued that the relationship between the extent of the invasion of corpus for purposes of supporting, educating, and maintaining the decedent's minor child, and the entirety of the corpus, was not expressed in "fractional or percentile" form and thus there was no "specific portion" for marital deduction purposes. The Second Circuit reviewed the use of actuarial formulas at some length and then finding for the taxpayer, remanded the case to the Tax Court to determine how much of the trust corpus qualified for the marital deduction under the actuarial principles which had been discussed. Though there was no mention of what particular formula should be applied, in either the Second Circuit's opinion or the stipulation of dismissal by the parties on the remand indicating the lump sum of the taxpayer's

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[15] 298 F.2d 544, 551 (2 Cir. 1962).

overpayment,[16] *Gelb* can easily be read to be consistent with the result for which the appellant contends in the instant case. Under the facts of *Gelb* only the life expectancies were subject to variation. By applying the $5,000 figure, the *maximum* extent to which the trustees could invade the trust corpus annually, together with the combined average figure of the surviving spouse's and minor child's life expectancies, the lump sum amount to be carved out of the trust corpus could be acceptably *maximized* by the computation. The remainder would be that part of the trust corpus, the "specific portion", to which the estate would be entitled to a marital deduction, a part of the corpus which in no reasonable event could be invaded for interests other than those of the surviving spouse.

The *Gelb* principles and disapproval of the Government's regulation are appropriate to the facts of *that* case. [fol. 61] But there is no need to take a position concerning the validity of that interpretive regulation, as it applies to this case. Suffice it to say, even assuming its invalidity, we have been unable to conceive of a method to compute the "specific portion" of the trust corpus to which the surviving spouse is entitled to all the income for her life. There are too many variables here. The market conditions for purposes of investment are unknown. If they are poor, a greater invasion of corpus to meet the monthly stipend will be necessary, causing a concomitant diminution of income. If market conditions are good corpus may not have to be invaded, and income accumulations may indeed accrue. Furthermore, the extent to which the appellee may, under Paragraph 12 of the will, choose to invade corpus for illness and financial emergencies is an unknown factor of considerable moment in any computation of "specific portion". Thus, in this case, the factual constants do not exist upon which the maximum income can be theoretically computed, as it was possible to theoretically compute the maximum invasion of corpus in *Gelb*. In

[16] See U.S. Tax Ct. Docket No. 71095, stipulation entered July 26, 1962.

short, the ratio between the maximum monthly income and the monthly stipend—the fraction of the entire corpus which would be the "specific portion" for marital deduction purposes—may not be acceptably computed.[17]

[fol. 62] In essence then, neither the District Court's formula, nor any other method of calculation of which we can conceive, when applied to the facts of this case, provides a method to handle the problem of maximizing the investment potential of the trust corpus. B cause the marital deduction is to be allowed only when the trust beneficiary has been given an interest akin to a fee simple, what *might* ultimately happen to the invested corpus is the central consideration in determining marital deduction qualification, and the ability to maximize future investment potential is crucial to qualification, absent a fractional or percentile expression of the right to income from the trust corpus. Thus, even if done with precision, the time of the decedent's death is the inappropriate time at which to freeze the income production status of the invested corpus for purposes of qualifying a "specific portion" for the marital deduction.

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[17] An illustration of an acceptable computation, given factual constants such as inhere in *Gelb*, is the following: If the investment factors involved were constant and it could be determined that the *maximum* income that could be produced from the corpus in a month was, for example, $500, then the relationship between the $300 monthly stipend and the $500 maximum income would define "specific portion" for marital deduction purposes, *i.e.*:

> $300 being 3/5 of $500 then 3/5 of $69,245.85 would be the "specific portion" of the trust corpus from which the surviving spouse would be entitled to the entire income of $300 monthly *under maximum production circumstances.*

Though in reality it might take the entire corpus to produce the monthly stipend, or even the necessity to invade corpus might be present, nevertheless, in line with *Gelb*, it could be said, after computing the theoretical maximum income, that the surviving spouse's income interest of $300 monthly represented the investment of 3/5 of the corpus. "Specific portion" would then be accurately defined for marital deduction purposes. Let it be re-emphasized, however, that the necessary constants are absent in the instant case upon which a computation may be based.

We have reached the above conclusion with an awareness that a three-judge panel of the Seventh Circuit has most recently expressed contrary views, one judge dissenting.[18] We think the observation of the dissenter, however, in characterizing the impact of the formula used in that case —"something judicially rationalized as approximately equivalent is not enough" [19]—is most appropriate. In our view, therefore, appellant's position is sustained.[20]

Sustaining the appellant's position is consistent with both the decedent's intent as expressed in his will and the purpose behind the marital deduction provision. The decedent's intent emerges rather clearly from Paragraph 11 of his will. In reciting that the monthly stipends were to be used exclusively for the survivor's sole and individual use, maintenance, and support, sums which he endeavored to make neither liable for any debts contracted by her, nor [fol. 63] subject to her assignment, the decedent evidenced a desire to limit the survivor's control over the monthly stipend. By also limiting the amount of these stipends to a sum which could fall below the income production of the corpus, the decedent evidenced an intent to give to his surviving spouse only that which he thought would be proper for her support and maintenance. Such an interest falls short of expressing a desire to place in the hands of his survivor an interest akin to a fee simple, the only interest which Congress viewed as meeting the standards of marital deduction status.

The judgment of the United States District Court for the Middle District of Pennsylvania will be reversed and

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[18] Citizens Nat'l Bank of Evansville, Exr. v. U.S., 2 Fed. Est. & Gift Tax Rep. § 12,394 at 8167-71 (April 11, 1966).

[19] *Id.* at 8171.

[20] For a like result under somewhat different facts see Flesher v. United States, 238 F. Supp. 119, 124 (N.D.W.Va. 1965). See 4 Mertens, Law of Federal Gift & Estate Taxation 145 (July 1965 Monthly Supp.).

the case remanded for entry of summary judgment in favor of appellant.

By GANEY, *Circuit Judge, dissenting.*

Clarence C. Young died on May 3, 1958. Surviving him were his widow, who was 42 years old at the time, and four children, whose ages are not disclosed by the record. He left a last will and testament in which the plaintiff was named executor and trustee of the estate. Item 6 thereof provided as follows:

> "ITEM 6. I give, devise and bequeath one-half (½) of all the rest, residue and remainder of my estate, whatsoever and wheresoever the same may be, both real and personal, to which I may be entitled, or which I may have power to dispose of at the time of my death, unto my Trustee, hereinafter named and designated, to have and to hold the same in trust, nevertheless, as hereinafter provided.
>
> "(a) I direct my Trustee to pay out of the said income and corpus of the said estate unto my wife, Beatrice O. Young, the sum of Three Hundred Dollars ($300.00) per month for and during the period until [fol. 64] my youngest child reaches the age of eighteen years and thereafter I direct my Trustee to pay to my wife, Beatrice O. Young, the sum of Three Hundred Fifty Dollars ($350.00) per month for and during the rest of her natural life.
>
> "(b) If my wife survives me, she shall have the power, exercisable by Will, to appoint to her estate or to others, any or all of the principal remaining at the time of her death. If my wife fails to appoint the entire principal to her estate or to others as above mentioned, then upon her death (or if she predeceases me, then upon my death) any principal remaining at that time shall be paid over to my children on the same terms and conditions as under Item 7 of this my Will."

It is to be noted that the surviving widow is to have the income from all of the trust estate, as well as the power of appointment over the same by her last will and testament as to all or any part thereof. At the time of the decedent's death, the value of the testamentary residuary trust passing under the will, to which all parties were in agreement, was $69,245.85. The widow also received outright from the decedent's estate at the time of his death, property and money valued at $41,751.02. One-half of the decedent's adjusted gross estate amounted to $99,874.98 and the executor of the estate reported this value as a marital deduction in the Federal estate tax return and took therein as a partial deduction the $41,751.02.

Section 2056(b)(5) of the Internal Revenue Code of 1954, 26 U.S.C. § 2056,[1] remedied previous legislation which [fol. 65] failed to provide for a situation in which the surviving spouse received an interest less than all of the trust income or the power to appoint less than all of the trust property, to the extent that, where the surviving spouse is entitled for life to all of the income from a "specific portion" thereof with power in the surviving spouse to appoint such "specific portion", it will qualify for the marital deduction. The phrase "specific portion" is nowhere defined in the statute, but Treasury Regulations on Estate

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[1] This section reads as follows:

"(5) *Life estate with power of appointment in surviving spouse.*—In the case of an interest in property passing from the decedent, if his surviving spouse is entitled for life to all the income from the entire interest, *or all the income from a specific portion* thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the interest, or such specific portion, to any person other than the surviving spouse. . . ." (Emphasis supplied.)

Tax (1954 Code), Sec. 20.2056(b)-5[2] so does, and therein it provides as set forth below that the surviving spouse's right to income must be a fractional or percentile share of the trust corpus.

The Commissioner of Internal Revenue disallowed any part of the $69,245.85, the value of the trust corpus to be included in the marital deduction and allowed only the $41,751.02, and assessed a deficiency estate tax of $14,966.23 plus interest at $2,608.22 against the estate. The executor paid the deficiency tax plus interest and brought this action in the United States District Court for the Middle District of Pennsylvania to recover those amounts. Both parties moved for summary judgment and the court below decided in favor of the executor in 235 F. Supp. 941, and the United States has prosecuted this appeal.

[fol. 66] It is the Government's contention here that (1) since the surviving spouse is not entitled to all the income from the entire corpus during her lifetime, because under

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[2] This section, in pertinent part, reads as follows:

"Marital Deduction; Life Estate with Power of Appointment in Surviving Spouse.

"(c) *Definition of 'specific portion'*. A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse in income and as to the power constitute a fractional or percentile share of a property interest so that such interest or share in the surviving spouse reflects its proportionate share of the increment or decline in the whole of the property interest to which the income rights and the power relate. Thus, if the right of the spouse to income and the power extend to one-half or a specified percentage of the property, or the equivalent, the interest is considered as a specific portion. On the other hand, if the annual income of the spouse is limited to a specific sum, or if she has a power to appoint only a specific sum out of a larger fund, the interest is not a deductible interest. Even though the rights in the surviving spouse may not be expressed in terms of a definite fraction or percentage, a deduction may be allowable if it is shown that the effect of local law is to give the spouse rights which are identical to those she would have acquired if the size of the share had been expressed in terms of a definite fraction or percentage . . . ."

the terms of the decedent's will income from the trust could have exceeded $300.00 per month and the surplus would then have to be accumulated and therefore the trust becomes disqualified.[3] Furthermore, (2) the $300.00 per month allotted as income to the widow is not in conformity with the Treasury Regulation cited above since it is not fractional or percentile and no part of it, accordingly, could qualify for the marital deduction. The court below is in agreement with the first portion of the Government's contention that the plaintiff is not entitled to take as a marital deduction the value of the property passing to the spouse under the testamentary residuary trust. However, on the other hand, the contention of the executor is that since the trust makes provision for setting up a monthly income to the surviving spouse, and she alone, under the will, was granted all of the income from the trust corpus, as well as being given power to dispose of all of her interest by appointment, the plaintiff was entitled to take as a marital deduction the value of the $300.00 per month as a "specific portion" as may be computed actuarially. Since the surviving spouse is absolutely entitled to, presently, $300.00 per month, and if this amount is construed to represent income from corpus, then the amount of the corpus which would yield this income could be ascertained and regarded as qualifying as a "specific portion" for the marital deduction. Here, the court rejects the Government's second contention and agrees with the above contention of the executor since the underlying purpose of Congress in enacting the marital deduction provision of the statute was that it might conform to the pattern of [fol. 67] state law in those states which permit transfer

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[3] See S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., p. 17 (1948-1 Cum. Bull. 285, 342-343), U. S. Code Cong. Service 1948, p. 1239: "(3) The surviving spouse must be entitled to the income from the corpus of the trust annually, or at more frequent intervals. This requirement disqualifies any trust the income of which is required to be accumulated or may, in the discretion of the trustee, be accumulated."

free of taxes of one-half of the known community property to the surviving spouse in what has been referred to as community property states. It is, accordingly, our duty to construe the statute as liberally as we can in order to effectuate such policy.

The value of this right was computed by multiplying together the following factors: $300.00 (amount of monthly payment); 12 (number of months in a year); 1.0159 (factor for monthly payments) and 17.3911 (factor for the discount rate of 3½% over the period of the widow's life expectancy). See Sec. 20.2031-7 of the Treasury Regulations of the Estate Tax provisions of the 1954 Internal Revenue Code, 26 C.F.R. Part 20-29 (Rev'd. 1961) Sec. 20.2031-7. *Citizens National Bank of Evansville* v. *United States,* (S.D. Ind. 1965), 65-1 USTC ¶ 12,302, a similar case, was decided in this way. This right had a value, according to this actuarial computation, of $63,663.43. The executors contend that this was a "specific portion" of the trust corpus and that the Treasury Regulation so far as it required a fractional or percentile part of the trust was invalid as being the only and exclusive indication of Congressional intent.

With this contention of the executor, I likewise agree. While, as I have indicated, all of the value of $69,245.85 could not be taken as a marital deduction, certainly $300.00 monthly for life devised in trust for his wife had a value at the time of his death and this value could be related to, or be a specific portion of, the entire corpus, and, as determined, it amounted to $63,663.43. This figure is reached after a reasonable calculation of the present worth of $300.00 over the life expectancy of the wife. I do not take into consideration fluctuation, wide or narrow, of the value of the corpus or the income thereon, over what would be the life expectancy of the wife, since the marital deduction is taken only once, at the death of testator, and I determine then what could be its value and not what might ultimately [fol. 68] happen. "We cannot wait, like Monday morning

quarterbacks, to see what actually happened, but must concern ourselves with what could have happened." *Bookwalter* v. *Lamar*, 232 F. 2d 664, 670.

It is in conformity with this that I do not take into consideration the $350.00 stipend somewhat later to be paid to the beneficiary, as it is prospective of an exigency which might never occur, and, as has been indicated, I take the marital deduction but once and at the date of the testator's death and hence the amount of the stipend at that time. This construction does not strain the statutory intent nor does it, in any wise, work a change in the phrase, "specific portion", and is fully in accord with the mandate of the statute that anyone seeking the marital deduction must satisfy the requirements thereof, which is the requisite rule in statutory construction. *United States* v. *Olympic Radio & Television*, 349 U.S. 232, 235; *Deputy* v. *Dupont*, 208 U.S. 488, 493; *New Colonial Ice Co.* v. *Helvering*, 292 U.S. 435, 440.

The final point of the majority here is an attempt to extract, from paragraph 11 of the testator's will, an intent by him to "limit the survivors' control over the monthly stipend", thus not making it akin to a fee simple.

Paragraph 11 merely provides that the fund created for the wife is for her "sole and separate use, maintenance and support" and not "only that which he thought would be proper for her support and maintenance", as stated by the majority.

As a matter of fact, this paragraph of the will has no real bearing on the issue here presented, for if the testator had provided a percentile interest for the wife, instead of a monthly stipend, this paragraph would have been equally applicable to it, so even if expressed in a percentile interest, the majority, taking the position they do here, would thus be defeating their own argument.

Since the wife gets all of the income from the specific portion and has the power of appointment over all of it, [fol. 69] this method of determining the specific portion of the corpus by evaluating the life interest at the time of the

testator's death is, in my judgment, neither inconsistent nor irreconcilable with the statutory requirement.

Furthermore, while this formula may not be a perfect one, its components are fair and reasonable and tested by Governmental experience and, therefore, it seems but just that some value be given the stipend at the testator's death in order to qualify for the marital deduction, in conformance with the desire of Congress to give full effect to its marital deduction in order that it might level off any inequality resulting from community property states, rather than let the field lie fallow and adopt a sterile attitude of defeatism because the testator has not resorted to fractional or percentile figures.

The value of the "specific portion" being ascertained at $63,663.43 within the intendment of the statute, plus the $41,757.02 already taken as a deduction, therefore exceeds the allowable marital deduction of $99,874.02, and therefore $58,117.00 of the $63,663.43, the value of the "specific portion", should be allowed additionally.

Accordingly, I would affirm the judgment of the lower court.

Chief Judge Staley and Judge McLaughlin join in this dissent.

[fol. 70]

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 15,249

NORTHEASTERN PENNSYLVANIA NATIONAL BANK & TRUST COMPANY, Executor Under the Will of CLARENCE C. YOUNG,

vs.

UNITED STATES OF AMERICA, Appellant.

(D. C. Civil No. 7993)

On appeal from the United States District Court for the Middle District of Pennsylvania.

Present: STALEY, *Chief Judge*, and MCLAUGHLIN, KALODNER, HASTIE, FORMAN, GANEY, SMITH and FREEDMAN, *Circuit Judges*.

JUDGMENT—July 19, 1966

This cause came on to be heard on the record from the United States District Court for the Middle District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the order of the District Court, filed September 30, 1964, be, and the same is hereby reversed and the case is remanded for entry of summary judgment in favor of appellant.

ATTEST:

Ida O. Creskoff, Clerk.

July 19, 1966

[fol. 71] Clerk's Certificate (omitted in printing).

[fol. 72]

SUPREME COURT OF THE UNITED STATES

No. 637—OCTOBER TERM, 1966

NORTHEASTERN PENNSYLVANIA NATIONAL BANK & TRUST COMPANY, etc., Petitioner,

v.

UNITED STATES.

ORDER ALLOWING CERTIORARI—December 5, 1966

The petition herein for a writ of certiorari to the United States Court of Appeals for the Third Circuit is granted, and the case is placed on the summary calendar.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1966

No. 637

NORTHEASTERN PENNSYLVANIA NATIONAL BANK & TRUST COMPANY, EXECUTOR UNDER THE WILL OF CLARENCE C. YOUNG, *Petitioner*,

v.

UNITED STATES OF AMERICA, *Respondent*.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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INDEX

CITATIONS

IN THE

Supreme Court of the United States

October Term, 1966

No.

Northeastern Pennsylvania National Bank & Trust Company, Executor Under the Will of Clarence C. Young, *Petitioner*,

v.

United States of America, *Respondent*.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit, entered in the above-entitled case on July 19, 1966.

CITATIONS TO OPINIONS BELOW

The opinion of the District Court is reported at 235 F. Supp. 941 (M.D. Pa. 1964). The opinion of the court of appeals (App. A, *infra*, pp. 1a-23a) is reported at F. 2d .

JURISDICTION

The judgment of the court of appeals was entered on July 19, 1966. The jurisdiction of this court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether the right in a widow to receive from a testamentary trust of her husband the sum of Three Hundred dollars ($300.00) per month for and during the period until his youngest child reaches the age of eighteen years, and thereafter the sum of Three Hundred Fifty dollars ($350.00) per month for and during the rest of her natural life, with the power to appoint all the remainder of the trust, qualified for the marital deduction as a "specific portion" of the trust within the meaning of Section 2056(b)(5) of the Internal Revenue Code of 1954.

2. Whether the provisions of Section 20.2056(b)(5) of the Treasury Regulations on Estate Tax (1954 Code) defining "specific portion" of the entire interest in property as a fractional or percentile share of such interest are in conflict with Section 2056(b)(5) of the 1954 Code and therefore invalid.

3. Whether, by use of a prescribed Treasury Department actuarial table, the present value of the "specific portion" of the trust can be feasibly computed in order to arrive equitably at a value to be used for estate tax purposes.

STATUTES AND REGULATIONS INVOLVED

Sections 2056(a), (b)(1), (b)(5), and (c) of the Internal Revenue Code of 1954 and portions of Treasury Regulations (1954 Code), §§ 20.2056(b)-5(a), (b), (c), (d) and (f) are set forth in App. B, *infra*, pp.

24a-32a. The most pertinent portion of the statute, § 2056(b)(5), provides that:

> [i]n the case of an interest in property passing from the decedent, if his surviving spouse is entitled for life to all the income from the entire interest, or all the income from a specific portion thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the interest, or such specific portion, to any person other than the surviving spouse * * *

the interest or such portion thereof shall qualify for the marital deduction.

STATEMENT

Clarence C. Young (the decedent) died testate on May 3, 1958, survived by his wife and four children. His last will and testament named the petitioner as executor and trustee of the estate. Item 6 of the decedent's last will and testament provides as follows:

> I give, devise and bequeath one-half (½) of all the rest, residue and remainder of my estate, whatsoever and wheresoever the same may be, both real and personal, to which I may be entitled, or which I may have the power to dispose of at the time of my death, unto my Trustee hereinafter named and designated, to have and to hold the same in trust, nevertheless, as hereinafter provided.
>
> (a) I direct that my Trustee pay out of the said income and corpus of the said estate unto my wife,

Beatrice O. Young, the sum of Three Hundred dollars ($300.00) per month for and during the period until my youngest child reaches the age of eighteen years, and thereafter I direct my Trustee to pay to my wife, Beatrice O. Young, the sum of Three Hundred Fifty dollars ($350.00) per month for and during the rest of her natural life.

(b) If my wife survives me, she shall have the power, exercisable by Will, to appoint to her estate, or to others, any or all of the principal remaining at the time of her death. If my wife fails to appoint the entire principal to her estate or to others as above authorized, then upon her death (or if she predeceases me, then upon my death) any principal remaining at that time shall be paid over to my children on the same terms and conditions as under Item 7 of this my Will.

The vlaue of the testamentary trust passing under Item 6 of the decedent's will was $69,245.85, which was listed on the estate tax return by the taxpayer (petitioner) as qualifying for the marital deduction pursuant to Section 2056 of the Internal Revenue Code of 1954. The value of the property passing outside the will, to the decedent's spouse, $41,751.02, was combined on the estate tax return with the full value of the testamentary residuary trust, $69,245.85, to total $110,996.87. The adjusted gross estate was $199,749.96, and the taxpayer (petitioner) claimed a marital deduction in the amount of $99,874.98, constituting one-half of the adjusted gross estate. The Government eliminated the full value of the testamentary residuary trust from the marital deduction as claimed and thus decreased the amount of the allowable marital deduction to

$41,751.02. The resulting deficiency in estate tax was paid, a claim for refund was disallowed, and this suit for refund was instituted in the District Court.

The District Court decided that the entire value of the trust corpus, $69,245.85, could not be considered for the marital deduction. Instead, it decided that the taxpayer (petitioner) was entitled to deduct as a marital deduction the value of the present worth of the surviving spouse's monthly stipend. The value arrived at, $63,663.43, which was based upon a Treasury Department actuarial formula, was added to $41,751.02, the value of the property passing to the surviving spouse outside the will, to total $105,414.45, an amount in excess of one-half of the decedent's adjusted gross estate, $99,874.98, the maximum allowable statutory marital deduction. The District Court thus concluded that the taxpayer (petitioner) was entitled to the full marital deduction of $99,874.98, and judgment was entered awarding the refund plus interest.

The Government, thereupon, appealed the case to the Court of Appeals for the Third Circuit, which Court reversed the decision of the District Court, three judges dissenting. The Third Circuit ruled that the value of the specific portion from which the wife would be entitled to all the income for life was not acceptably computed. It held that the specific portion need not be a stated fractional or percentile share, but that it is necessary that it be feasible to compute the amount of the specific portion, which, it felt, could not be done in this particular case.

REASONS FOR GRANTING THE WRIT

1. The instant decision is in direct conflict with the decision of the Court of Appeals for the Seventh Circuit in *The Citizens National Bank of Evansville* v. *United States,* 359 F. 2d 817 (March 31, 1966) which case was referred to in the majority opinion of Judge Forman in the instant case (F. 2d at) wherein he stated his awareness that the three judge panel of the Seventh Circuit, one judge dissenting, had recently expressed contrary views, thereby creating a direct conflict.

The facts of the two cases are substantially identical. In both cases a decedent created a residuary trust under which his surviving spouse was to receive a fixed dollar amount per month payable either out of income or corpus, and with a general power of appointment in the surviving spouse over the remainder of the trust estate at her death. The question in each of the two cases was whether the trust was entitled to a marital deduction under Code § 2056(b)(5). In the instant case, the Third Circuit, sitting *en banc,* denied the claimed deduction, three judges dissenting. By contrast, in *The Citizens National Bank of Evansville* v. *United States,* the Seventh Circuit allowed the deduction, one judge dissenting. The Seventh Circuit held that the qualifying specific portion of the trust corpus could be computed by capitalizing the widow's fixed monthly payment at an annual yield of 3½ percent. The Third Circuit, however, concluded that no method of computation could feasibly compute the amount of the specific portion in that particular case.

It is essential that the Court review the decisions of the two lower courts in order that the tax laws of the United States may be uniformly applied.

2. Clearly, the questions presented are of importance in the administration of the Internal Revenue laws. Congress enacted Code § 2056 permitting the marital deduction in order to equalize the effect of estate taxes in community property and common law jurisdictions. *United States* v. *Stapf,* 375 U.S. 118, 128; *Jackson* v. *United States,* 376 U.S. 503, 511. § 2056(b)(1), (b)(5) was later enacted to permit the marital deduction benefit where a decedent created a trust in favor of his surviving spouse whereby she would be entitled for life to all the income from the entire interest, or all the income from a specific portion thereof with a general power to appoint the entire interest, or such specific portion. Where such a marital deduction is allowed, the effect is to defer the estate tax on that property interest until the death of the surviving spouse, at which time such property interest would be included in that person's gross estate for tax purposes.

The disallowance of the marital deduction in this particular case enables the Government to defeat the intention of Congress. § 2056(b)(5), as enacted, does not define the term "specific portion", whereas the Treasury Regulations § 20.2056(b)-(5)(c) of the 1954 Internal Revenue Code defines specific portion as follows:

> "A partial interest in property is not treated as a specific portion of the entire interest unless the right of the surviving spouse in income and as to the power constitute a fractional or percentile share of a property interest so that such interest or share in the surviving spouse reflects its proportionate share of the increment or decline in the whole of the property to which the income rights and the power relate."

Nowhere in § 2056(b)(5) of the Internal Revenue Code of 1954 (26 U.S.C. 1958 ed., Sec. 2056(b)(5)) or in its legislative history (S. Rep. No. 1622, 83rd Cong., 2d Sess., p. 125 3 U.S.C. Cong. & Adm. News (1954) 4621, 4758); H. Rep. No. 1337, 83rd Cong., 2d Sess., p. 91 (3 U.S.C. Cong. & Adm. News (1954) 4017, 4018)), is the term "specific portion" so narrowly defined to mean a "fractional or percentile share" of a property interest. If such was the intent of Congress, it is reasonable to suppose that it would have used such words in § 2056(b)(5) rather than the broader term "specific portion". The Second Circuit Court of Appeals in *Gelb* v. *Commissioner,* 298 F. 2d 544 (1962), agreed, wherein it stated at p. 551, "[T]hat Congress gave a fractional interest as an example of a 'specific portion' does not warrant a construction that Congress did not mean to include other instances fairly within the language and the underlying policy. We *disapprove* Regulations . . . § 20.2056(b)-5(c) insofar as it would limit a 'specific portion' to a 'fractional or percentile' share" (emphasis added). This language was subsequently adopted and referred to by the District Court in the instant case, 235 F. Supp. at 946, and by the Seventh Circuit Court of Appeals in *Citizens National Bank of Evansville* v. *United States,* 359 F. 2d at 821. In *Gelb,* the Second Circuit further stated, ". . . Congress spoke of a 'specific portion', not of a 'fractional or percentile share', and nowhere indicated any policy that deductibility of a 'specific portion' should be governed by the possibility that the spouse's portion will change in value relatively more or less than the clearly nonqualifying part."

It is of interest to note that there appears to be an inconsistency between the regulation involved in the

instant case and Section 20.2056(b)-6(e)(1) of the Treasury Regulations on Estate Tax[1] which deals with the marital deduction on life insurance payments. There is a different wording in Section 20.2056(b)-6 (e)(1) which tends to relax the application of the Code to insurance, as opposed to other property, where it should be equally relaxed.

It is of importance in the administration of the tax laws that the Supreme Court review the cases as pronounced by the lower courts, and the Treasury Regulations prescribed by the Government in order to insure that the legislative intent of the Congress is carried out.

3. The decision of the court below is believed to be erroneous and the conflicting decision of the Seventh Circuit Court of Appeals in *The Citizens National Bank of Evansville* v. *United States* correct. The court below, while not specifically ruling that the Treasury Regulations were void, stated that "it was unable to conceive of a method to compute the 'specific

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[1] § 20.2056(b)-6 *Marital deduction; life insurance or annuity payments with power of appointment in surviving spouse.*

(e) Applicable principles. (1) The principles set forth in paragraph (c) of § 20.2056(b)-5 for determining what constitutes a "specific portion of the entire interest" for the purpose of section 2056(b)(5) are applicable in determining what constitutes a "specific portion of all such amounts" for the purpose of section 2056(b)(6). However, the interest in the proceeds passing to the surviving spouse will not be disqualified by the fact that the installment payments or interest to which the spouse is entitled or the amount of the proceeds over which the power of appointment is exercisable may be expressed in terms of a specific sum rather than a fraction or a percentage of the proceeds provided it is shown that such sums are a definite or fixed percentage or fraction of the total proceeds.

portion' of the trust corpus. . . ." This decision was based upon the erroneous assumptions that there are too many variables involved in order to accurately compute such a present value, and that the time of the decedent's death is not the appropriate time at which to make such a determination to qualify a "specific portion" for the marital deduction. The marital deduction can be taken only once, at the time of the decedent's death, and there is no appropriate time other than the date of death, at which to compute the valuation necessary to permit the deduction. This position is emphasized by dissenting Judge Ganey.

It should be noted that the formula used by the District Court, which was rejected by the Third Circuit Court of Appeals, was one prescribed by the Treasury Department in its Regulation on Estate Tax § 20.2031-7. The use of actuarial tables, such as the one employed, has been widely used for Estate Tax purposes by the Commissioner and by taxpayers and is a reasonable method by which one can place a present value on interests such as the one presented by this case. The extent of such use is clearly set forth in footnote 7 of the *Gelb* opinion, 298 F. 2d at 551, which reads as follows:

> The use of life expectancy tables was sanctioned by the Commissioner in the 1863 edition of "Boutwell's Manual" at p. 203, in the context of a group of regulations which, according to Carlton Fox, "appear to embody the first that were promulgated in respect of taxes on legacies." Since the federal succession tax enacted in 1862 was an inheritance tax, see Warren & Surrey, Federal Estate and Gift Taxation (1961 ed.), p. 2, it was necessary to value legacies individually, and for that purpose the 1863 regulations provided that

remainders and life annuities should "be estimated by Carlisle's, or other approved tables of life annuities." As the regulations grew more elaborate, the Commissioner added examples to aid in applying the life tables "in ascertaining the values of life and reversionary interests," Instructions Concerning the Tax on Legacies, Distributive Shares, and Successions, pp. 24-25 (Series 7-No. 3, 1878). The change to the estate tax concept in the Revenue Act of 1916, c. 463, 39 Stat. 756, and its immediate successor, the Revenue Act of 1918, c. 18, 40 Stat. 1057, was accompanied by contemporaneous acceptance of the use of life expectancy tables to value "annuities, life, and remainder interests," art. 20, Regulations 37 (1919 ed.).

Introduction of the charitable deduction to the estate tax in § 403(a)(3) of the 1918 Act, 40 Stat. at 1098, led to instant acquiescence in the use of mortality tables to value charitable remainders, art. 53, Regulations 37 (1919 ed.). Perhaps their most frequent use in this area is to compute a gift to charity made subject to a life estate, see Merchants National Bank v. Commissioner, 320 U.S. 256, 259 [31 AFTR 753] fn. 6 (1943); Commissioner v. Estate of Sternberger, 348 U.S. 187, 190-192 [46 AFTR 976] (1955). The Supreme Court has even gone so far as to compel their use for such a computation when the life tenant had died before the case came to the Court, Ithaca Trust Co. v. United States, 279 U.S. 151 [7 AFTR 8856] (1929). See generally 4 Mertens, Law of Federal Gift and Estate Taxation (1959), § 28.30.

Other uses of mortality tables in Federal taxation are manifold. A typical application under the estate tax occurs if a vested remainderman dies before the life beneficiary, William Korn, 35 B. T. A. 1071 (1937). For purposes of the gift tax, they are used to value gifts of remainders, Henry F. duPont, 2 T. C. 246 (1943); Betty Du-

maine, 16 T. C. 1035 (1951), and of life estates and annuities, F. J. Sensenbrenner, 46 B. T. A. 713 (1942). They have long been utilized to value annuities, not only for estate and gift tax purposes, but to allocate between return of capital and incremental return for income tax purposes. See GCM 8826, C. B. IX-2, p. 194 (1930); Florence L. Klein, 6 B. T. A. 617 (1927); Guaranty Trust Co., 15 B. T. A. 20 (1929); Estate of Sarah A. Bergan, 1 T. C. 543 (1943). They are used also to derive the "adjusted uniform basis," the 1954 Codes' way of splitting basis between life tenant and remainderman in the event, for instance, either wishes to sell his interest while both are still alive. See Regs. § 1.1014-5(a)(1); 3A Mertens, Law of Federal Income Taxation (Zimet & Weiss rev. vol. 1958), § 21.71, at p. 200.

The Second Circuit in *Gelb,* in referring to actuarial formulas, 298 F. 2d at 551, stated "the use of actuarial tables for dealing with estate tax problems has been so widespread and of such long standing that we cannot assume Congress would have balked at it here; the United States is in business with enough different taxpayers so that the law of averages has ample opportunity to work."

The "variables" which the Third Circuit referred to should not be taken into consideration in the calculation of the value of the "specific portion". This is because the marital deduction *is* taken only once, at the death of the testator, and we can only concern ourselves with what is its value and not with what will happen. It is therefore unreasonable to assume that the method used by the District Court in calculating the specific portion is inconsistent or irreconcilable with the statutory requirement.

CONCLUSION

We submit that the intent of the Congress in enacting Section 2056(b)(5) of the Internal Revenue Code to provide a marital deduction is frustrated by the ruling of the majority of the Third Circuit in this case. Under its approach the estate is subject to an additional "tax bite" and upon the death of the widow the balance in the trust will also be subject to a "tax bite". Congress did not intend this whip-saw.

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

MILTON I. BALDINGER
DONALD J. FENDRICK
Attorneys

October, 1966

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 15249

NORTHEASTERN PENNSYLVANIA NATIONAL BANK & TRUST COMPANY, EXECUTOR UNDER THE WILL OF CLARENCE C. YOUNG

v.

UNITED STATES OF AMERICA, *Appellant*

Appeal From the United States District Court for the Middle District of Pennsylvania

Argued October 18, 1965

Reargued June 9, 1966

Before STALEY, *Chief Judge*, and MCLAUGHLIN, KALODNER, HASTIE, FORMAN, GANEY, SMITH, and FREEDMAN, *Circuit Judges*

Opinion of the Court

(Filed July 19, 1966)

By FORMAN, *Circuit Judge*.

This is an appeal by the defendant, United States of America (hereinafter appellant) from a summary judgment entered by the United States District Court for the Middle District of Pennsylvania on the motion of plaintiff, Northeastern Pennsylvania Bank and Trust Company,

Executor under the will of Clarence C. Young (hereinafter appellee), in the amount of $17,574.45 with interest, and from the denial of appellant's motion for summary judgment. Appellee's suit alleged an improper rejection of a claimed marital deduction.

Decedent died testate on May 3, 1958 survived by his wife and four children. Paragraph 6 of decedent's will [1] provided for the bequest of one-half of the residue of the estate to appellee who was directed to pay out of income, and corpus if necessary, the sum of $300 per month to decedent's wife until his youngest child reached eighteen years of age, after which appellee was directed to pay decedent's wife $350 per month for the rest of her life. Paragraph 6 also provided that if decedent's wife survived him, she would have the power, exercisable by will, to appoint to her estate, or to others, any or all of the

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[1] "ITEM 6. I give, devise and bequeath one-half (½) of all the rest, residue and remainder of my estate, whatsoever and wheresoever the same may be, both real and personal, to which I may be entitled, or which I may have power to dispose of at the time of my death, unto my Trustee hereinafter named and designated, to have and to hold the same in trust, nevertheless, as hereinafter provided.

> "(a) I direct my Trustee to pay out of the said income and corpus of the said estate unto my wife, Beatrice O. Young, the sum of Three Hundred Dollars ($300.00) per month for and during the period until my youngest child reaches the age of eighteen years, and thereafter I direct my Trustee to pay to my wife, Beatrice O. Young, the sum of Three Hundred Fifty Dollars ($350.00) per month for and during the rest of her natural life.
>
> "(b) If my wife survives me, she shall have the power, exercisable by Will, to appoint to her estate, or to others, any or all of the principal remaining at the time of her death. If my wife fails to appoint the entire principal to her estate or to others as above authorized, then upon her death (or if she predeceases me, then upon my death) any principal remaining at that time shall be paid over to my children on the same terms and conditions as under Item 7 of this my Will."

principal of the trust remaining at the time of her death. Paragraph 11 [2] recited that such stipends were in no event to be liable for any debts contracted by the survivor and were not to be liable to attachment or assignment, but were solely for the use, maintenance and support of the survivor.[3] Paragraph 11 also indicated that income produced from the corpus of the trust which exceeds the monthly allotment is to be accumulated. Paragraph 12 [4] of the will granted appellee the power to authorize payments over and above the monthly stipend up to $1500 in the event of a serious illness or financial emergency affecting the surviving spouse. Whether the figure of $1500 is in the aggregate or may be paid in each event is unclear.

Decedent's adjusted gross estate was $199,749.96. Appellee sought to qualify the maximum amount, one-half of that adjusted gross estate, $99,874.98, as a marital deduc-

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[2] "ITEM 11. The income and payments herein provided for my wife and children and the issue of my children are for their, and each of their, sole and separate use, maintenance and support, and are in no event to be liable for any debts contracted by them or any of them, and are not to be liable to attachment or assignment, but are solely and exclusively for their and each of their sole and individual use, maintenance and support, and none of the income and payments shall vest in the said cestuis que trustent, or either of them, until payments shall have been made to her or to him, as the case may be."

[3] Whether such limitations are valid has no bearing here as we are only interested in them as they reflect the decedent's intent.

[4] "ITEM 12. In the event of a serious illness or a financial emergency affecting my wife or any of my children, I herewith direct and authorize my Trustee to pay, in addition to other payments hereinbefore provided for, to my wife, or to my children, as the case may be, an amount not exceeding Fifteen Hundred Dollars ($1500.00), the said amount to be determined by my Trustee, as in its discretion the same may be necessary, during such illness or financial difficulty. The said payments to any child or children to be considered as an advancement and to be deducted, from the respective share of said child or children."

tion in accordance with Sections 2056(c)(1)[5] and 2056(b)(5)[6] of the 1954 Internal Revenue Code. The value of the property passing outside the will, to the decedent's spouse, $41,751.02, was combined on the estate tax return with the full value of the testamentary residuary trust, $69,245.85, to total $110,996.87. That portion of $110,996.87 which constituted one-half of the adjusted gross estate, $99,874.98, was listed, as noted above, as qualifying for the marital deduction. Appellant eliminated the full value of the testamentary residuary trust from the claimed marital deduction and thus decreased the amount of the allowable marital deduction to $41,751.02. The deficiency in estate tax was paid, a claim for refund was disallowed, appellee filed suit for refund, and after motions for summary judgment were presented by both parties, the District Court ruled in favor of the appellee and granted the refund.[7]

The District Court did not, as proposed by appellee, conclude that the entire value of the trust corpus, $69,245.85, could be considered for the marital deduction. Instead, it applied a Treasury Department actuarial formula to value the present worth of the surviving spouse's monthly stipend. This formula produced a value of $63,663.43. This was added to $41,751.02, the value of the property passed to the surviving spouse outside the will, to total $105,414.45, an amount in excess of one-half of the decedent's adjusted gross estate, $99,874.98, the maximum allowable statutory marital deduction. The District Court thus concluded that appellee was entitled to the full marital deduction of $99,874.98, and judgment was entered for $17,574.45 plus interest, representing the tax found to have been unlawfully collected by appellant.

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[5] 26 U.S.C. § 2056(c)(1) (1965).

[6] 26 U.S.C. § 2056(b)(5) (1965).

[7] Northeastern Pennsylvania Nat. B. & T. Co. v. United States, 235 F. Supp. 941 (M.D. Pa. 1964).

As the marital deduction provisions function today, under a trust arrangement such as the one involved herein, the entire corpus of the trust qualifies for inclusion in the estate tax return as part of the marital deduction if each of two prerequisites[8] are met: (1) the surviving spouse is entitled to all the income produced from the corpus for the remainder of the survivor's life with (2) power in the survivor to appoint the entire corpus remaining at the time of the power's exercise. If the survivor's requisite relationship to the corpus bars the qualification of the entire corpus for the deduction, a part of the trust corpus will qualify for marital deduction status if the survivor is entitled to the income from a "specific portion" of the whole, whether there be a power to appoint the entire interest remaining at the time of the power's exercise or the power to appoint only a part thereof.[9] Appellant's administrative regulation[10] has defined "specific portion" as a fractional or percentile part of the entire corpus. The practical effect of the marital deduction is to defer taxation of some part of the decedent's estate passing to the surviving spouse until the death of the surviving spouse.

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[8] There are other contingencies not relevant to the problem at hand.

[9] Consistent with this, only a part of the corpus will qualify for marital deduction status if the survivor is entitled to all the income from the corpus for life but may only appoint a "specific portion" of the remainder of the corpus at the time of the power's exercise. Similarly, only a part of the corpus, the smaller of the two specific portions, will qualify for marital deduction status if only a "specific portion" of the income may go to the survivor for life and if the survivor's power of appointment is limited to a "specific portion" of the remaining corpus at the time of the power's exercise. See 26 C.F.R. § 20.2056(b)-5(b) (1961).

[10] 26 C.F.R. § 20.2056(b)-5(b) (1961).

Reviewing the purpose of the marital deduction, Mr. Justice Goldberg speaking for a unanimous court in *United States* v. *Stapf*[11] explained:

> "The 1948 tax amendments were intended to equalize the effect of the estate taxes in community property and common-law jurisdictions.[12] [Footnote omitted.] Under a community property system, such as that in Texas, the spouse receives outright ownership of one-half of the community property and only the other one-half is included in the decedent's estate. To equalize the incidence of progressively scaled estate taxes and to adhere to the patterns of state law, the marital deduction permits a deceased spouse, subject to certain requirements, to transfer free of taxes one-half of the non-community property to the surviving spouse. Although applicable to separately held property in a community property state, the primary thrust of this is to extend to taxpayers in common-law states the advantages of 'estate splitting' otherwise available only in community property States."

Problems that have arisen in this area have in the main concerned the extent to which the advantages of estate-splitting are to be allowed. Towards clarification of this issue, the above noted interpretive regulation was promulgated. A detailed discussion of the congressional intent behind the passage of the 1948 Revenue Act appears in Senate Report No. 1013, March 16, 1948 [to accompany H.R. 4790]. In that Report, the marital deduction additions to the 1949 Code are characterized as follows:

> "These provisions have the effect of allowing a marital deduction with respect to the value of prop-

[11] 375 U.S. 118, 128 (text and n. 12) (1963).

[12] 2 U.S. Code Cong. and Ad. News, 80th Cong., 2nd Session, p. 1238 (1948) (Emphasis added.)

erty transferred in trust or at the direction of the decedent *where the surviving spouse,* by reason of her right to the income and a power of appointment, *is the virtual owner of the property.*"[12]

And, as above detailed, the virtual ownership interest encompasses that existent in a "specific portion" of the trust corpus.

In sum, the propriety of granting a marital deduction in this case must be measured by the purpose of the marital deduction as expressed in *Stapf,* the interpretive regulation as promulgated by the Internal Revenue Service, the expression of the congressional intent on the subject, and the decedent's intent in structuring the existent trust arrangement.

II

As the survivor has been given in Paragraph 6 the right to appoint the entire corpus, no question arises in this case concerning the "specific portion" of the corpus to which the power extends. The contentions concern solely the relationship between the survivor's monthly stipend and the trust corpus—whether the decedent's trust arrangement placed in his surviving spouse the right to all the income from the corpus, or all the income from a "specific portion" thereof? The appellee has offered alternative arguments, as it did before the District Court, to justify either the inclusion of the entire $69,245.85 residuary trust in the estate tax return as appropriate for marital deduction status or the inclusion of $63,663.43 in the return as a "specific portion" of the residuary trust thus qualifying for marital deduction status.

The District Court rejected, properly we believe, appellee's contention that the entirety of the trust corpus of $69,245.85 be entitled to marital deduction status. It was pointed out that appellee's position fails for, in de-

ciding whether the survivor is entitled to receive all the income from the trust corpus for life, the determinative factor is what income the trust corpus *could* produce and not what is *now* being produced, or what ultimately *will* be produced. Here, the corpus may be able to produce more than the survivor's monthly stipend. The surplus would have to be accumulated and the survivor would have no right to the *present enjoyment* of the excess income, even though, as argued by appellee, she would have the power to appoint it. Thus, the survivor would not be entitled to the entire income which might come from the corpus, within the intendment of Section 2056(b)(5) of the 1954 Internal Revenue Act.[13] This very real consideration must also be given appropriate weight in determining whether the survivor is entitled to the income from a "specific portion" of the trust, and what such "specific portion" is.

Was appellee, as found by the District Court, entitled to the inclusion in its tax return of $63,663.43 from the corpus as a "specific portion" thereof—a part in which the surviving spouse had a total income interest? The method of actuarial computation used by the District Court, along with the efficacy of the use of any actuarial method of computing "specific portion", is of primary concern and requires analysis. It is well to underline the statutory language which must be considered in this respect. Section 2056(b)(5) of the Code makes it clear that "specific portion" is that part of the trust corpus from which the sur-

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[13] It should be noted in passing that it would be unrealistic to conceive of an unlimited income potential from a trust whose trustees, by law, must stay within the bounds of certain guidelines. Such a consideration may play a part in another case at another time. Here, however, appellee does not argue, nor does the record reflect, that the appellee, by law, cannot invest the corpus to produce an income in excess of the monthly stipend. Thus the potentiality of the production of an income in excess of the monthly stipend to the survivor is a real factor which has been, and must be, given its due weight by the courts.

viving spouse is entitled to "all the income." Thus, unless the actuarial formula used by the District Court succeeds in isolating that part of the trust corpus from which the survivor is entitled to *all* the income for her lifetime, the computation is of no value. The actuarial method on which this case has been turned does not, in our view, isolate that part of the trust corpus from which the surviving spouse is entitled all the income.

The District Court, in computing the present worth of the survivor's monthly stipend, applied a formula used by the Treasury Department in the "valuation of annuities, life estates, terms for years, remainders and reversions." This may be found in 26 C.F.R. § 20.2031-7 (1961). The formula valued the worth of the monthly stipends by multiplying together the following factors: \$300 (amount of monthly payment); 12 (number of months in a year); 1.0159 (factor for monthly payments); and 17.3911 (factor for the discount rate of 3½ percent over the period of the widow's life expectancy). The present worth of the \$300 monthly stipend was determined to be \$63,663.43, a "specific portion" of the trust corpus, and thus qualifying for marital deduction status. The District Court thus rejected the Treasury Regulation noted above so far as it required the "specific portion" to be specified in fractional or percentile form.

As an initial matter, we find the formula inappropriate in determining what part of a trust corpus may be considered a "specific portion" for marital deduction purposes. First, the mere fact that the formula is one for valuing an annuity eliminates it as appropriate for determining "specific portion." The factor 17.3911 in the formula represents the present worth of one dollar invested in an annuity at 3½ percent over the remaining life expectancy of a person forty-two years of age, the age of the surviving spouse at the decedent's death. The formula thus provides a discount value through a process of capitalizing at 3½ percent what are directed to be \$300

monthly payments. If $63,663.43 is invested at age forty-two, that amount will provide the annuitant the required monthly payments for her entire life. At death the entire fund will have been dissipated. However, the factor of fund dissolution has in no way been contemplated by the decedent. The formula thus intrudes an artificial element into our problem, an element inconsistent with what the District Court in effect conceded to be the income production potential of the corpus when it ruled that appellee was not entitled to a marital deduction for the full value of the trust corpus.

Second, the monthly stipend alloted under the trust arrangement, $300 initially, is placed into the formula as the amount of *income* which a given fund must produce. However, under the trust arrangement, the trustees have not been directed to invest the corpus so that it will yield a given monthly income. All that has been directed is that the survivor receive such income, *even if corpus must be invaded* to make up the difference between the income yield of the corpus per month and the stipend allotment. And if the income yield be greater than $300 in a given month, the excess is to be accumulated. Thus, inclusion of the $300 figure in the formula is inappropriate for it equates the monthly stipend with the income yield from the corpus, elements which are in no way interchangeable.

Third, and this has a direct bearing on the point just made, the formula may be characterized as one which attempts to capitalize a given monthy stipend and produce a capital value, $63,663.43, which is to be the "specific portion" for marital deduction purposes. Such a method of computation is improper for we already know what is the value of the entire trust. Only from that given value of $69,245.85 may any computation of "specific portion", if any be appropriate, proceed. Under the formula used by the District Court, the results that may be reached demonstrate the inappropriateness of a capitalization method which disregards the present value of the trust corpus.

Assume for a moment a direction that appellee pay $350 monthly as a stipend to the surviving spouse as of the date of decedent's death. Capitalizing a $350 monthly stipend under the District Court's formula for determining "specific portion", the capital value figure reached is $74,199.80, a sum in excess of the value of the entire trust corpus. As stated above it is conceded that the estate is not entitled to a marital deduction for the sum of the entire trust corpus, because of the potentialities of income production. Yet, under the actuarial formula used to determine "specific portion", the formula accepted by the District Court, at least the entire value of the corpus is to qualify for the deduction as a "specific portion" of the entirety, and theoretically a sum in excess of the entire trust corpus's value will qualify. The incongruity of equating the monthly stipend with the income yield is manifest.

Finally, in determining the "specific portion" of a given trust corpus from which part the survivor has an absolute income right, actuarial computation is inappropriate when the formula uses variable factors other than mere life expectancy. The use of the monthly stipend as the income factor in the formula noted above exemplifies the attempt to make constant that which is variable in this case. The 3½ percent investment factor in the actuarial formula is likewise unreal. As previously indicated, Congress's intent was to give a marital deduction to those interests of a surviving spouse in a common-law jurisdiction which were akin to the fee simple interest held by a survivor in a community property state. Such an interest, to qualify as akin to a fee simple interest, must be subject to the rise and fall of the market. An investment constant, such as 3½ percent in the instant case, though accepted in actuarial formulas, has no place in a problem where the very real income variations turn the issue of the allowance of the marital deduction. Indeed, the use of such a constant is absent from the regulations dealing with the "specific portion" issue, whereas it may be found in the regulations in formulas geared to different problems.

Having attempted to demonstrate the inappropriateness of the formula used by the District Court, the question arises as to whether, under the facts of this case, there does exist a method for isolating a "specific portion" of the trust corpus to qualify for marital deduction status? The term "specific portion" has been appropriately defined in this manner:

> "Presumably, specific portion does not mean anything more than a designation of the amount of the surviving spouse's interest *which makes it feasible to compute the amount of the marital deduction.*" [14]

Feasible computation of a "specific portion" is the key to marital deduction status.

The Internal Revenue Service in its above noted regulation considers any testamentary trust which describes the relationship between the income to be received by the survivor and the trust corpus in anything but "fractional or percentile" terms as one which expresses a relationship falling outside the susceptibility of computation, and thus one which thwarts a determination of "specific portion" for purposes of the marital deduction. *Gelb* v. *C.I.R.*,[15] heavily relied upon by appellee and the District Court, expressed a view which is contrary to the interpretive regulation. In *Gelb* the surviving spouse was entitled to *all* the income from the trust corpus for her life. As distinguished from the case at hand, the issue in *Gelb* was whether the survivor had a power of appointment over a "specific portion" of the trust corpus. That problem arose because the trustees in *Gelb* were empowered to invade the corpus, in their discretion, to the extent of $5,000 per year for the support, education and maintenance of the decedent's minor daughter. The Government argued that the

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[14] Lowndes and Kramer, Federal Estate and Gift Taxes 407 (1956). (Emphasis added.)

[15] 298 F. 2d 544, 551 (2 Cir. 1962).

relationship between the extent of the invasion of corpus for purposes of supporting, educating, and maintaining the decedent's minor child, and the entirety of the corpus, was not expressed in "fractional or percentile" form and thus there was no "specific portion" for marital deduction purposes. The Second Circuit reviewed the use of actuarial formulas at some length and then finding for the taxpayer, remanded the case to the Tax Court to determine how much of the trust corpus qualified for the marital deduction under the actuarial principles which had been discussed. Though there was no mention of what particular formula should be applied, in either the Second Circuit's opinion or the stipulation of dismissal by the parties on the remand indicating the lump sum of the taxpayer's overpayment,[16] *Gelb* can easily be read to be consistent with the result for which the appellant contends in the instant case. Under the facts of *Gelb* only the life expectancies were subject to variation. By applying the $5,000 figure, the *maximum* extent to which the trustees could invade the trust corpus annually, together with the combined average figure of the surviving spouse's and minor child's life expectancies, the lump sum amount to be carved out of the trust corpus could be acceptably *maximized* by the computation. The remainder would be that part of the trust corpus, the "specific portion", to which the estate would be entitled to a marital deduction, a part of the corpus which in no reasonable event could be invaded for interests other than those of the surviving spouse.

The *Gelb* principles and disapproval of the Government's regulation are appropriate to the facts of *that* case. But there is no need to take a position concerning the validity of that interpretive regulation, as it applies to this case. Suffice it to say, even assuming its invalidity, we have been unable to conceive of a method to compute the "specific

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[16] See U.S. Tax Ct. Docket No. 71095, stipulation entered July 26, 1962.

portion" of the trust corpus to which the surviving spouse is entitled to all the income for her life. There are too many variables here. The market conditions for purposes of investment are unknown. If they are poor, a greater invasion of corpus to meet the monthly stipend will be necessary, causing a concomitant diminution of income. If market conditions are good corpus may not have to be invaded, and income accumulations may indeed accrue. Furthermore, the extent to which the appellee may, under Paragraph 12 of the will, choose to invade corpus for illness and financial emergencies is an unknown factor of considerable moment in any computation of "specific portion". Thus, in this case, the factual constants do not exist upon which the maximum income can be theoretically computed, as it was possible to theoretically compute the maximum invasion of corpus in *Gelb*. In short, the ratio between the maximum monthly income and the monthly stipend—the fraction of the entire corpus which would be the "specific portion" for marital deduction purposes—may not be acceptably computed.[17]

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[17] An illustration of an acceptable computation, given factual constants such as inhere in *Gelb*, is the following: If the investment factors involved were constant and it could be determined that the *maximum* income that could be produced from the corpus in a month was, for example, $500, then the relationship between the $300 monthly stipend and the $500 maximum income would define "specific portion" for marital deduction purposes, *i.e.:*

> $300 being 3/5 of $500 then 3/5 of $69,245.85 would be the "specific portion" of the trust corpus from which the surviving spouse would be entitled to the entire income of $300 monthly *under maximum production circumstances.*

Though in reality it might take the entire corpus to produce the monthly stipend, or even the necessity to invade corpus might be present, nevertheless, in line with *Gelb*, it could be said, after computing the theoretical maximum income, that the surviving spouse's income interest of $300 monthly represented the investment of 3/5 of the corpus. "Specific portion" would then be accurately defined for marital deduction purposes. Let it be re-emphasized, however, that the necessary constants are absent in the instant case upon which a computation may be based.

In essence then, neither the District Court's formula, nor any other method of calculation of which we can conceive, when applied to the facts of this case, provides a method to handle the problem of maximizing the investment potential of the trust corpus. Because the marital deduction is to be allowed only when the trust beneficiary has been given an interest akin to a fee simple, what *might* ultimately happen to the invested corpus is the central consideration in determining marital deduction qualification, and the ability to maximize future investment potential is crucial to qualification, absent a fractional or percentile expression of the right to income from the trust corpus. Thus, even if done with precision, the time of the decedent's death is the inappropriate time at which to freeze the income production status of the invested corpus for purposes of qualifying a "specific portion" for the marital deduction.

We have reached the above conclusion with an awareness that a three-judge panel of the Seventh Circuit has most recently expressed contrary views, one judge dissenting.[18] We think the observation of the dissenter, however, in characterizing the impact of the formula used in that case—"something judicially rationalized as approximately equivalent is not enough"[19]—is most appropriate. In our view, therefore, appellant's position is sustained.[20]

Sustaining the appellant's position is consistent with both the decedent's intent as expressed in his will and the purpose behind the marital deduction provision. The decedent's intent emerges rather clearly from Paragraph

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[18] *Citizens Nat'l Bank of Evansville, Exr.* v. *U.S.*, 2 Fed. Est. & Gift Tax Rep. § 12,394 at 8167-71 (April 11, 1966).

[19] *Id.* at 8171.

[20] For a like result under somewhat different facts see *Flesher* v. *United States*, 238 F. Supp. 119, 124 (N.D. W. Va. 1965). See 4 Mertens, Law of Federal Gift & Estate Taxation 145 (July 1965 Monthly Supp.).

11 of his will. In reciting that the monthly stipends were to be used exclusively for the survivor's sole and individual use, maintenance, and support, sums which he endeavored to make neither liable for any debts contracted by her, nor subject to her assignment, the decedent evidenced a desire to limit the survivor's control over the monthly stipend. By also limiting the amount of these stipends to a sum which could fall below the income production of the corpus, the decedent evidenced an intent to give to his surviving spouse only that which he thought would be proper for her support and maintenance. Such an interest falls short of expressing a desire to place in the hands of his survivor an interest akin to a fee simple, the only interest which Congress viewed as meeting the standards of marital deduction status.

The judgment of the United States District Court for the Middle District of Pennsylvania will be reversed and the case remanded for entry of summary judgment in favor of appellant.

By Ganey, *Circuit Judge, dissenting.*

Clarence C. Young died on May 3, 1958. Surviving him were his widow, who was 42 years old at the time, and four children, whose ages are not disclosed by the record. He left a last will and testament in which the plaintiff was named executor and trustee of the estate. Item 6 thereof provided as follows:

> "Item 6. I give, devise and bequeath one-half (½) of all the rest, residue and remainder of my estate, whatsoever and wheresoever the same may be, both real and personal, to which I may be entitled, or which I may have power to dispose of at the time of my death, unto my Trustee, hereinafter named and desig-

nated, to have and to hold the same in trust, nevertheless, as hereinafter provided.

"(a) I direct my Trustee to pay out of the said income and corpus of the said estate unto my wife. Beatrice O. Young, the sum of Three Hundred Dollars ($300.00) per month for and during the period until my youngest child reaches the age of eighteen years and thereafter I direct my Trustee to pay to my wife, Beatrice O. Young, the sum of Three Hundred Fifty Dollars ($350.00) per month for and during the rest of her natural life.

"(b) If my wife survives me, she shall have the power, exercisable by Will, to appoint to her estate or to others, any or all of the principal remaining at the time of her death. If my wife fails to appoint the entire principal to her estate or to others as above mentioned, then upon her death (or if she predeceases me, then upon my death) any principal remaining at that time shall be paid over to my children on the same terms and conditions as under Item 7 of this my Will."

It is to be noted that the surviving widow is to have the income from all of the trust estate, as well as the power of appointment over the same by her last will and testament as to all or any part thereof. At the time of the decedent's death, the value of the testamentary residuary trust passing under the will, to which all parties were in agreement, was $69,245.85. The widow also received outright from the decedent's estate at the time of his death, property and money valued at $41,751.02. One-half of the decedent's adjusted gross estate amounted to $99,874.98 and the executor of the estate reported this value as a marital deduction in the Federal estate tax return and took therein as a partial deduction the $41,751.02.

Section 2056(b)(5) of the Internal Revenue Code of 1954, 26 U.S.C. § 2056,[21] remedied previous legislation which failed to provide for a situation in which the surviving spouse received an interest less than all of the trust income or the power to appoint less than all of the trust property, to the extent that, where the surviving spouse is entitled for life to all of the income from a "specific portion" thereof with power in the surviving spouse to appoint such "specific portion", it will qualify for the marital deduction. The phrase "specific portion" is nowhere defined in the statute, but Treasury Regulations on Estate Tax (1954 Code), Sec. 20.2056(b)-5 [22] so does, and therein

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[21] This section reads as follows:

"(5) *Life estate with power of appointment in surviving spouse.*—In the case of an interest in property passing from the decedent, if his surviving spouse is entitled for life to all the income from the entire interest, *or all the income from a specific portion* thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the interest, or such specific portion, to any person other than the surviving spouse. * * *" [Emphasis supplied.]

[22] This section, in pertinent part, reads as follows:

"Marital Deduction; Life Estate with Power of Appointment in Surviving Spouse.

"(c) *Definition of 'specific portion'.* A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse in income and as to the power constitute a fractional or percentile share of a property interest so that such interest or share in the surviving spouse reflects its proportionate share of the increment or decline in the whole of the property interest to which the income rights and the power relate. Thus, if the right of the spouse to income and the power extend to one-half or a specified percentage of the property, or the equivalent, the

it provides as set forth below that the surviving spouse's right to income must be a fractional or percentile share of the trust corpus.

The Commissioner of Internal Revenue disallowed any part of the $69,245.85, the value of the trust corpus to be included in the marital deduction and allowed only the $41,751.02, and assessed a deficiency estate tax of $14,966.23 plus interest at $2,608.22 against the estate. The executor paid the deficiency tax plus interest and brought this action in the United States District Court for the Middle District of Pennsylvania to recover those amounts. Both parties moved for summary judgment and the court below decided in favor of the executor in 235 F. Supp. 941, and the United States has prosecuted this appeal.

It is the Government's contention here that (1) since the surviving spouse is not entitled to all the income from the entire corpus during her lifetime, because under the terms of the decedent's will income from the trust could have exceeded $300.00 per month and the surplus would then have to be accumulated and therefore the trust becomes disqualified.[23] Furthermore, (2) the $300.00 per

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interest is considered as a specific portion. On the other hand, if the annual income of the spouse is limited to a specific sum, or if she has a power to appoint only a specific sum out of a larger fund, the interest is not a deductible interest. Even though the rights in the surviving spouse may not be expressed in terms of a definite fraction or percentage, a deduction may be allowable if it is shown that the effect of local law is to give the spouse rights which are identical to those she would have acquired if the size of the share had been expressed in terms of a definite fraction or percentage * * *."

[23] See S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., p. 17 (1948—1 Cum. Bull. 285, 342-343), U.S. Code Cong. Service 1948, p. 1239: "(3) The surviving spouse must be entitled to the income from the corpus of the trust annually, or at more frequent intervals. This requirement disqualifies any trust the income of which is required to be accumulated or may, in the discretion of the trustee, be accumulated."

month allotted as income to the widow is not in conformity with the Treasury Regulation cited above since it is not fractional or percentile and no part of it, accordingly, could qualify for the marital deduction. The court below is in agreement with the first portion of the Government's contention that the plaintiff is not entitled to take as a marital deduction the value of the property passing to the spouse under the testamentary residuary trust. However, on the other hand, the contention of the executor is that since the trust makes provision for setting up a monthly income to the surviving spouse, and she alone, under the will, was granted all of the income from the trust corpus, as well as being given power to dispose of all of her interest by appointment, the plaintiff was entitled to take as a marital deduction the value of the $300.00 per month as a "specific portion" as may be computed actuarily. Since the surviving spouse is absolutely entitled, to, presently, $300.00 per month, and if this amount is construed to represent income from corpus, then the amount of the corpus which would yield this income could be ascertained and regarded as qualifying as a "specific portion" for the marital deduction. Here, the court rejects the Government's second contention and agrees with the above contention of the executor since the underlying purpose of Congress in enacting the marital deduction provision of the statute was that it might conform to the pattern of state law in those states which permit transfer free of taxes of one-half of the known community property to the surviving spouse in what has been referred to as community property states. It is, accordingly, our duty to construe the statute as liberally as we can in order to effectuate such policy.

The value of this right was computed by multiplying together the following factors: $300.00 (amount of monthly payment); 12 (number of months in a year); 1.0159 (factor for monthly payments) and 17.3911 (factor for the discount rate of 3½% over the period of the widow's life

expectancy). See Sec. 20.2031-7 of the Treasury Regulations of the Estate Tax provisions of the 1954 Internal Revenue Code, 26 C.F.R. Part 20-29 (Rev'd. 1961) Sec. 20.2031-7. *Citizens National Bank of Evansville* v. *United States,* (S.D. Ind. 1965), 65-1 USTC ¶ 12,302, a similar case was decided in this way. This right had a value, according to this actuarial computation, of $63,663.43. The executors contend that this was a "specific portion" of the trust corpus and that the Treasury Regulation so far as it required a fractional or percentile part of the trust was invalid as being the only and exclusive indication of Congressional intent.

With this contention of the executor, I likewise agree. While, as I have indicated, all of the value of $69,245.85 could not be taken as a marital deduction, certainly $300.00 monthly for life devised in trust for his wife had a value at the time of his death and this value could be related to, or be a specific portion of, the entire corpus, and, as determined, it amounted to $63,663.43. This figure is reached after a reasonable calculation of the present worth of $300.00 over the life expectancy of the wife. I do not take into consideration fluctuation, wide or narrow, of the value of the corpus or the income thereon, over what would be the life expectancy of the wife, since the marital deduction is taken only once, at the death of testator, and I determine then what could be its value and not what might ultimately happen. "We cannot wait, like Monday morning quarterbacks, to see what actually happened, but must concern ourselves with what could have happened." *Bookwalter* v. *Lamar*, 232 F. 2d 664, 670.

It is in conformity with this that I do not take into consideration the $350.00 stipend somewhat later to be paid to the beneficiary, as it is prospective of an exigency which might never occur, and, as has been indicated, I take the marital deduction but once and at the date of the testator's

death and hence the amount of the stipend at that time. This construction does not strain the statutory intent nor does it, in any wise, work a change in the phrase, "specific portion", and is fully in accord with the mandate of the statute that anyone seeking the marital deduction must satisfy the requirements thereof, which is the requisite rule in statutory construction. *United States* v. *Olympic Radio & Television*, 349 U.S. 232, 235; *Deputy* v. *Dupont*, 208 U.S. 488, 493; *New Colonial Ice Co.* v. *Helvering*, 292 U.S. 435, 440.

The final point of the majority here is an attempt to extract, from paragraph 11 of the testator's will, an intent by him to "limit the survivors' control over the monthly stipend", thus not making it akin to a fee simple.

Paragraph 11 merely provides that the fund created for the wife is for her "sole and separate use, maintenance and support" and not "only that which he thought would be proper for her support and maintenance", as stated by the majority.

As a matter of fact, this paragraph of the will has no real bearing on the issue here presented, for if the testator had provided a percentile interest for the wife, instead of a monthly stipend, this paragraph would have been equally applicable to it, so even if expressed in a percentile interest, the majority, taking the position they do here, would thus be defeating their own argument.

Since the wife gets all of the income from the specific portion and has the power of appointment over all of it, this method of determining the specific portion of the corpus by evaluating the life interest at the time of the testator's death is, in my judgment, neither inconsistent nor irreconcilable with the statutory requirement.

Furthermore, while this formula may not be a perfect one, its components are fair and reasonable and tested by Governmental experience and, therefore, it seems but

just that some value be given the stipend at the testator's death in order to qualify for the marital deduction, in conformance with the desire of Congress to give full effect to its marital deduction in order that it might level off any inequality resulting from community property states, rather than let the field lie fallow and adopt a sterile attitude of defeatism because the testator has not resorted to fractional or percentile figures.

The value of the "specific portion" being ascertained at \$63,663.43 within the intendment of the statute, plus the \$41,757.02 already taken as a deduction, therefore exceeds the allowable marital deduction of \$99,874.02, and therefore \$58,117.00 of the \$63,663.43, the value of the "specific portion", should be allowed additionally.

Accordingly, I would affirm the judgment of the lower court.

Chief Judge Staley and Judge McLaughlin join in this dissent.

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit.

APPENDIX B

Internal Revenue Code of 1954:

SEC. 2056. BEQUESTS, ETC., TO SURVIVING SPOUSE.

(a) *Allowance of Marital Deduction*—For purposes of the tax imposed by section 2001, the value of the taxable estate shall, except as limited by subsections (b), (c) and (d) be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

(b) *Limitation in the Case of Life Estate or Other Terminable Interest.*—

(1) *Genral rule.*—Where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an ev[illegible] or contingency to occur, an interest passing to the surviving spouse will terminate or fail, no deduction shall be allowed under this section with respect to such interest—

(A) if an interest in such property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to any person other than such surviving spouse (or the estate of such spouse); and

(B) if by reason of such passing such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest so passing to the surviving spouse;

and no deduction shall be allowed with respect to such interest (even if such deduction is not disallowed under subparagraphs (A) and (B))—

(C) if such interest is to be acquired for the surviving spouse, pursuant to directions of the decedent, by his executor or by the trustee of a trust.

For purposes of this paragraph, an interest shall not be considered as an interest which will terminate or fail merely because it is the ownership of a bond, note, or similar contractual obligation, the discharge of which would not have the effect of an annuity for life or for a term.

* * * * * * * * *

(5) *Life estate with power of appointment in surviving spouse.*—In the case of an interest in property passing from the decedent, if his surviving spouse is entitled for life to all the income from the entire interest, or all the income from a specific portion thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the interest, or such specific portion, to any person other than the surviving spouse—

(A) the interest or such portion thereof so passing shall, for purposes of subsection (a), be considered as passing to the surviving spouse, and

(B) no part of the interest so passing shall, for purposes of paragraph (1)(A), be considered as passing to any person other than the surviving spouse.

This paragraph shall apply only if such power in the surviving spouse to appoint the entire interest,

or such specific portion thereof, whether exercisable by will or during life, is exercisable by such spouse alone and in all events.

*   *   *   *   *   *   *   *   *

(c) *Limitation on Aggregate of Deductions.*—

(1) *General rule.*—The aggregate amount of the deductions allowed under this section (computed without regard to this subsection) shall not exceed 50 percent of the value of the adjusted gross estate, as defined in paragraph (2).

(2) *Computation of adjusted gross estate.*—

(A) *General rule.*—Except as provided in subparagraph (B) of this paragraph, the adjusted gross estate shall, for purposes of subsection (c) (1), be computed by subtracting from the entire value of the gross estate the aggregate amount of the deductions allowed by sections 2053 and 2054.

(B) *Special rule in cases involving community property.*—If the decedent and his surviving spouse at any time, held property as community property under the law of any State, Territory, or possession of the United States, or of any foreign country, then the adjusted gross estate shall, for purposes of subsection (c)(1), be determined by subtracting from the entire value of the gross estate the sum of—

(i) the value of property which is at the time of the death of the decedent held as such community property;

*   *   *   *   *   *   *   *   *

[26 U.S.C. (1958 ed.) Sec. 2056.]

Treasury Regulation on Estate Tax (1954 Code):

Sec. 20.2056(b)-5 Marital deduction; life estate with power of appointment in surviving spouse.

(a) *In general.* Section 2056(b)(5) provids that if an interest in property passes from the decedent to his surviving spouse (whether or not in trust) and the spouse is entitled for life to all the income from the entire interest or all the income from a specific portion of the entire interest, with a power in her to appoint the entire interest or the specific portion, the interest which passes to her is a deductible interest, to the extent that it satisfies all five of the conditions set forth below (see paragraph (b) of this section if one or more of the conditions is satisfied as to only a portion of the interest):

(1) The surviving spouse be entitled for life to all of the income from the entire interest or a specific portion of the entire interest, or to a specific portion of all the income from the entire interest.

(2) The income payable to the surviving spouse must be payable annually or at more frequent intervals.

(3) The surviving spouse must have the power to appoint the entire interest or the specific portion to either herself or her estate.

(4) The power in the surviving spouse must be exercisable by her alone and (whether exercisable by will or during life) must be exercisable in all events.

(5) The entire interest or the specific portion must not be subject to a power in any other person to appoint any part to any person other than the surviving spouse.

(b) *Specific portion; deductible amount.* If either the right to income or the power of appointment passing to the surviving spouse pertains only to a specific

portion of a property interest passing from the decedent, the marital deduction is allowed only to the extent that the rights in the surviving spouse meet all of the five conditions described in paragraph (a) of this section. While the rights over the income and the power must coexist as to the same interest in property, it is not necessary that the rights over the income or the power as to such interest be in the same proportion. However, if the rights over income meeting the required conditions set forth in paragraph (a) (1) and (2) of this section extend over a smaller share of the property interest than the share with respect to which the power of appointment requirements set forth in paragraph (a) (3) through (5) of this section are satisfied, the deductible interest is limited to the smaller share. Correspondingly, if a power of appointment meeting all the requirements extends to a smaller portion of the property interest than the portion over which the income rights pertain, the deductible interest cannot exceed the value of the portion to which such power of appointment applies. Thus, if the decedent leaves to his surviving spouse the right to receive annually all of the income from a particular property interest and a power of appointment meeting the specifications prescribed in paragraph (a) (3) through (5) of this section as to only one-half of the property interest, then only one-half of the property interest is treated as a deductible interest. Correspondingly, if the income interest of the spouse satisfying the requirements extends to only one-fourth of the property interest and a testamentary power of appointment satisfying the requirements extends to all of the property interest, then only one-fourth of the interest in the spouse qualifies as a deductible interest. Further, if the surviving spouse has no right to income from a specific portion of a property interest but a testamentary power of appointment which meets the necessary conditions over

the entire interest, then none of the interest qualifies for the deduction. In addition, if, from the time of the decedent's death, the surviving spouse has a power of appointment meeting all of the required conditions over-three-fourths of the entire property interest and the prescribed income rights over the entire interest, but with a power in another person to appoint one-half of the entire interest, the value of the interest in the surviving spouse over only one-half of the property interest will qualify as a deductible interest.

(c) *Definition of "specific portion".* A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse in income and as to the power constitute a fractional or percentile share of a property interest so that such interest or share in the surviving spouse reflects its proportionate share of the increment or decline in the whole of the property interest to which the income rights and the power relate. Thus, if the right of the spouse to income and the power extend to one-half or a specified percentage of the property, or the equivalent, the interest is considered as a specific portion. On the other hand, if the annual income of the spouse is limited to a specific sum, or if she has a power to appoint only a specific sum out of a larger fund, the interest is not a deductible interest. Even though the rights in the surviving spouse may not be expressed in terms of a definite fraction or percentage, a deduction may be allowable if it is shown that the effect of local law is to give the spouse rights which are identical to those she would have acquired if the size of the share had been expressed in terms of a definite fraction or percentage. The following examples illustrate the application of this and the preceding paragraphs of this section:

Example (1). The decedent transferred to a trustee 500 identical shares of X Company stock. He pro-

vided that during the lifetime of the surviving spouse the trustee should pay her annually one-half of the trust income or $6,000, which ever is the larger. The spouse was also given a general power of appointment exercisable by her last will over the sum of $160,000 or over three-fourths of the trust corpus, whichever should be of larger value. Since there is no certainty that the trust income will not vary from year to year, for purposes of paragraphs (a) and (b) of this section, an annual payment of a specified sum, such as the $6,000 provided for in this case, is not considered as representing the income from a definite fraction or a specific portion of the entire interest if that were the extent of the spouse's interest. However, since the spouse is to receive annually at least one-half of the trust income, she will, for purposes of paragraphs (a) and (b) of this section, be considered as receiving all of the income from one-half of the entire interest in the stock. Inasmuch as there is no certainty that the value of the stock will be the same on the date of the surviving spouse's death as it was on the date of decedent's death, for purposes of paragraphs (a) and (b) of this section, a specified sum, such as the $160,000 provided for in this case, is not considered to be a definite fraction of the entire interest. However, since the surviving spouse has a general power of appointment over at least three-fourths of the trust corpus, she is considered as having a general power of appointment over three-fourths of the entire interest in the stock.

* * * * * * * * *

(d) *Definition of "entire interest".* Since a marital deduction is allowed for each qualifying separate interest in property passing from the decedent to his surviving spouse (subject to the percentage limitation contained in §§ 20.2056 (c)-1 and 20.2056 (c)-2 concerning the aggregate amount of the deductions), for

purposes of paragraphs (a) and (b) of this section, each property interest with respect to which the surviving spouse received some rights is considered separately in determining whether her rights extend to the entire interest or to a specific portion of the entire interest. A property interest which consists of several identical units of property (such as a block of 250 shares of stock, whether the ownership is evidenced by one or several certificates) is considered one property interest, unless certain of the units are to be segregated and accorded different treatment in which case each segregated group of items is considered a separate property interest. The bequest of a specified sum of money constitutes the bequest of a separate property interest if immediately following distribution by the executor and thenceforth it, and the invesments made with it, must be so segregated or accounted for as to permit its identification as a separate item of property. The application of this paragraph may be illustrated by the following examples:

Example (*1*). The decedent transferred to a trustee three adjoining farms, Blackacre, White acre, and Greenacre. His will provided that during the lifetime of the surviving spouse the trustee should pay her all of the income from the trust. Upon her death, all of Blackacre, a one-half interest in Whiteacre, and a one-third interest in Greenacre were to be distributed to the person or persons appointed by her in her will. The surviving spouse is considered as being entitled to all of the income from the entire interest in Blackacre, all of the income from the entire interest in Whiteacre, and all of the income from the entire interest in Greenacre. She also is considered as having a power of appointment over the entire interest in Blackacre, over one-half of the entire interest in Whiteacre, and over one-third of the entire interest in Greenacre.

Example (*2*). The decedent bequeathed $250,000 to C, as trustee. C is to invest the money and pay all of the income from the investments to W, the decedent's surviving spouse, annually. W was given a general power, exercisable by will, to appoint one-half of the corpus of the trust. Here, immediately following distribution by the executor, the $250,000 will be sufficiently segregated to permit its identification as a separate item, and the $250,000 will constitute an entire property interest. Therefore, W has a right to income and a power of appointment such that one-half of the entire interest is a deductible interest.

Example (*3*). The decedent bequeathed 100 shares of Z Corporation stock to D, as trustee. W, the decedent's surviving spouse, is to receive all of the income of the trust annually and is given a general power, exercisable by will, to appoint out of the trust corpus the sum of $25,000. In this case the $25,000 is not, immediately following distribution, sufficiently segregated to permit its identificaton as a separate item of property in which the surviving spouse has the entire interest. Therefore, the $25,000 does not constitute the entire interest in a property for the purpose of paragraphs (a) and (b) of this section.

* * * * * * * * *

(f) *Right to income.* * * * (7) An interest passing in trust fails to satisfy the condition set forth in paragraph (a)(1) of this section, that the spouse be entitled to all the income, to the extent that the income is required to be accumulated in whole or in part or may be accumulated in the discretion of any person other than the surviving spouse * * *.

* * * * * * * * *

[26 C.F.R. Sec. 20.2056(b)-5.]

In the Supreme Court of the United States

OCTOBER TERM, 1966

No. 637

NORTHEASTERN PENNSYLVANIA NATIONAL BANK & TRUST CO., EXECUTOR, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

MEMORANDUM FOR THE UNITED STATES

Decedent died on May 3, 1958. His will devised one half of the residue of his estate to petitioner as trustee and directed it to pay out of income, and corpus if necessary, $300 per month to his widow until his youngest child reached the age of eighteen years and thereafter to pay her $350 per month for life. Decedent's will also gave his widow a testamentary power "to appoint to her estate, or to others, any or all of the [trust] principal remaining at the time of her death." (Pet. 3–4.)

The question presented is whether part or all of the $69,245 testamentary trust corpus qualifies for the estate tax marital deduction. This in turn depends on whether decedent's widow, in addition to hav-

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ing a general power of appointment over the trust corpus, was also entitled "for life to all the income from the entire interest, or *all the income from a specific portion* thereof, payable annually or at more frequent intervals." 1954 Code, § 2056(b)(5) (emphasis added).

The district court concluded that it could, by actuarial calculations, isolate the portion of the trust corpus from which the widow would be entitled to "all the income," and it set this amount at $63,663.43 (R. 22a–34a [1]). The Court of Appeals for the Third Circuit, sitting *en banc,* reversed by a vote of 5 to 3 (Pet. 1a–23a). It explicitly recognized that its decision conflicted with a recent decision of the Seventh Circuit in *Citizens National Bank of Evansville* v. *United States,* 359 F. 2d 817, in which the government has filed a petition for certiorari, No. 488, this term.

The Third Circuit concluded that where a decedent placed property in trust and directed that a fixed dollar amount be paid periodically to his widow, it was impossible to compute what portion of the corpus would be necessary to produce the fixed periodic amounts. Because the rates of return might fluctuate markedly over the widow's lifetime, an amount which would, in one year, produce the stated fixed amount might, in other years, produce far more or far less. Therefore, no computation could isolate any "specific portion" of the corpus from which the widow would, during her life, receive "all the income." The court declined to follow the Seventh Circuit's *Citizens Na-*

[1] "R." references are to the printed appendix to the government's brief in the court of appeals.

tional Bank decision and disallowed the claimed marital deduction.

We believe that the instant decision is correct. As explained in our petition for certiorari in *Citizens National Bank, supra,* Congress' purpose in enacting § 2056(b)(5) was to give a marital deduction only when the decedent made his widow "the virtual owner" of a portion of the trust property. S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., p. 16. Where the decedent gives her the right to only fixed periodic payments from the trust, so that her income will not rise and fall as the income of the trust fluctuates, she is not "the virtual owner" of "a specific portion" of the property. Since decedent's widow in this case was not entitled to "all the income" from either the entire property or a specific portion thereof, the lower court correctly denied the marital deduction.

In view of the direct conflict between the circuits on an issue of importance to estate planners, however, we believe that it would be appropriate for the Court to grant the instant petition, together with the government's petition in No. 488 which presents the same issue.

Respectfully submitted.

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OCTOBER 1966.

U.S. GOVERNMENT PRINTING OFFICE: 1966

FILED
JAN 31 1967
JOHN F. DAVIS, CLE

No. 637

IN THE

Supreme Court of the United States

OCTOBER TERM, 1966

NORTHEASTERN PENNSYLVANIA NATIONAL BANK & TRUST COMPANY, EXECUTOR UNDER THE WILL OF CLARENCE C. YOUNG, *Petitioner,*

v.

UNITED STATES OF AMERICA, *Respondent.*

On Writ of Certiorari to the United States Court of Appeals for the Third Circuit

---

BRIEF FOR THE PETITIONER

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PRESS OF BYRON S. ADAMS PRINTING, INC., WASHINGTON, D. C.

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BRIEF FOR THE PETITIONER

CITATIONS TO OPINIONS BELOW

The opinion of the District Court (R. 17-27) is reported at 235 F. Supp. 941 (M.D. Pa. 1964). The opinion of the court of appeals and the dissent thereto (R. 38-59) is reported at 363 F. 2d 476.

JURISDICTION

The judgment of the court of appeals was entered on July 19, 1966 (R. 60). The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether the right in a widow to receive from a testamentary trust of her husband the sum of Three Hundred dollars ($300.00) per month for and during the period until his youngest child reaches the age of eighteen years, and thereafter the sum of Three Hundred Fifty dollars ($350.00) per month for and during the rest of her natural life, with the power to appoint all the remainder of the trust, qualified for the marital deduction as a "specific portion" of the trust within the meaning of Section 2056(b)(5) of the Internal Revenue Code of 1954.

2. Whether the provisions of Section 20.2056(b)-5 of the Treasury Regulations on Estate Tax (1954 Code) defining "specific portion" of the entire interest in property as a fractional or percentile share of such interest are in conflict with Section 2056(b)(5) of the 1954 Code and therefore invalid.

3. Whether, by use of a prescribed Treasury Department actuarial table, the present value of the "specific portion" of the trust can be feasibly computed in order to arrive equitably at a value to be used for estate tax purposes.

STATUTES AND REGULATIONS INVOLVED

Sections 2056(a), (b)(1), (b)(5), and (c) of the Internal Revenue Code of 1954 and portions of Treasury Regulations (1954 Code), §§ 20.2056(b)-5(a), (b), (c), (d) and (f) may be found in the Record, pp. 28-35. The most pertinent portion of the statute, § 2056(b)(5), provides that:

> [i]n the case of an interest in property passing from the decedent, if his surviving spouse is en-

> titled for life to all the income from the entire interest, or all the income from a specific portion thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the interest or such specific portion, to any person other than the surviving spouse * * *

the interest or such portion thereof shall qualify for the marital deduction.

STATEMENT

Clarence C. Young (the decedent) died testate on May 3, 1958, survived by his wife and four children. His last will and testament (R. 7-11) named the petitioner as executor and trustee of the estate. Item 6 of the decedent's last will and testament provides as follows (R. 8-9):

> I give, devise and bequeath one-half (½) of all the rest, residue and remainder of my estate, whatsoever and wheresoever the same may be, both real and personal, to which I may be entitled, or which I may have the power to dispose of at the time of my death, unto my Trustee hereinafter named and designated, to have and to hold the same in trust, nevertheless, as hereinafter provided.
>
> (a) I direct that my Trustee pay out of the said income and corpus of the said estate unto my wife, Beatrice O. Young, the sum of Three Hundred dollars ($300.00) per month for and during the

period until my youngest child reaches the age of eighteen years, and thereafter I direct my Trustee to pay to my wife, Beatrice O. Young, the sum of Three Hundred Fifty dollars ($350.00) per month for and during the rest of her natural life.

(b) If my wife survives me, she shall have the power, exercisable by Will, to appoint to her estate, or to others, any or all of the principal remaining at the time of her death. If my wife fails to appoint the entire principal to her estate or to others as above authorized, then upon her death (or if she predeceases me, then upon my death) any principal remaining at that time shall be paid over to my children on the same terms and conditions as under Item 7 of this my Will.

The value of the testamentary trust passing under Item 6 of the decedent's will was $69,245.85, which was listed on the estate tax return by the taxpayer (petitioner) as qualifying for the marital deduction pursuant to Section 2056 of the Internal Revenue Code of 1954. The value of the property passing outside the will, to the decedent's spouse, $41,751.02, was combined on the estate tax return with the full value of the testamentary residuary trust, $69,245.85, to total $110,996.87. The adjusted gross estate was $199,749.96, and the taxpayer (petitioner) claimed a marital deduction in the amount of $99,874.98, constituting one-half of the adjusted gross estate. The Government eliminated the full value of the testamentary residuary trust from the marital deduction as claimed and thus decreased the amount of the allowable marital deduction to $41,751.02. The resulting deficiency in estate tax was paid, a claim for refund was disallowed, and this suit

for refund was instituted in the District Court (R. 4-15).

The District Court decided that the entire value of the trust corpus, $69,245.85, could not be considered for the marital deduction (R. 23). Instead, it decided that the taxpayer (petitioner) was entitled to deduct as a marital deduction the value of the present worth of the surviving spouse's monthly stipend. The value arrived at, $63,663.43, which was based upon a Treasury Department actuarial formula, was added to $41,751.02, the value of the property passing to the surviving spouse outside the will, to total $105,414.45, an amount in excess of one-half of the decedent's adjusted gross estate, $99,874.98, the maximum allowable statutory marital deduction (R. 26). The District Court thus concluded that the taxpayer (petitioner) was entitled to the full marital deduction of $99,874.98, and judgment was entered awarding the refund plus interest (R. 26-27).

The Government, thereupon, appealed the case to the Court of Appeals for the Third Circuit, which Court reversed the decision of the District Court, three judges dissenting (R. 38-59). The Third Circuit ruled that the value of the specific portion from which the wife would be entitled to all the income for life was not acceptably computed. It held that the specific portion need not be a stated fractional or percentile share, but that it is necessary that it be feasible to compute the amount of the specific portion, which, it felt, could not be done in this particular case.

INTRODUCTION AND SUMMARY OF ARGUMENT

Congress originally enacted Code § 2056 permitting the marital deduction in order to equalize insofar as possible the effect of estate taxes in community property and common law jurisdictions. Section 2056(b)(5) was later enacted to permit the marital deduction benefit where a decedent creates a trust in favor of his surviving spouse whereby she would be entitled for life to all the income from the entire interest, or all the income from a *specific portion* thereof with a general power to appoint the entire interest, or such specific portion. Where such a marital deduction is allowed, the effect is to defer the estate tax on that property interest until the death of the surviving spouse, at which time such property interest would be included in that person's gross estate for tax purposes.

Section 2056(b)(5), as enacted, does not define the term "specific portion", whereas the Treasury Regulations § 20.2056(b)-5(c) defines specific portion as follows:

> "A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse in income and as to the power constitute a fractional or percentile share of a property interest so that such interest or share in the surviving spouse reflects its proportionate share of the increment or decline in the whole of the property interest to which the income rights and the power relate. * * *"

The Third Circuit's majority in the case at bar casts some doubt upon the limitation adopted in the Regulations narrowing the right of the surviving spouse in income and as to the power to a fractional or percentile share (R. 50), while other courts, including the Second

and Seventh Circuits, have disapproved the limitation and have held the Regulations invalid.

The remainder of the widow's trust will be included in her gross estate upon her death for Federal Estate Tax purposes since she has a general power of appointment and Congress could not have had an intent to have its policy frustrated by a narrow limitation in the Regulations and thus put a double "tax bite" on what testator had built up—once, at his death, and again on the death of his spouse.

It has been held by this Court and other courts that qualification for the marital deduction is determined as at the date of the decedent's death. Yet, the majority opinion of the Third Circuit appears to go beyond this in an attempt to shore up its conclusion and negates this aspect when it says:

> "Thus, even done with precision, the time of the decedent's death is the inappropriate time at which to freeze the income production status of the invested corpus for purposes of qualifying a 'specific portion' for the marital deduction." (R. 51)

Reading the will of the testator demonstrates very clearly that the draftsman of the will and the testator who executed the same wanted to qualify the widow's trust for the marital deduction. Yet the majority opinion of the Third Circuit in order to buttress its conclusion finds other language in the will to find an intent of the testator to militate against the marital deduction.

In attacking the use of the actuarial table, in determining the spec fic portion, the majority opinion of the Third Circuit states that the factor of fund dissolu-

tion has in no way been contemplated by the decedent (R. 46). We submit that something is being read into the decedent's intent which the language of Item 6 in the will setting up the widow's trust dissipates. Item 6(a) of the will (R. 8-9) clearly provides that the Trustee is to pay to the wife of decedent out of income and corpus the sum of $300 a month until the youngest child reaches the age of eighteen years and $350 thereafter "during the rest of her natural life." Additionally, the wife is given the "power, exercisable by Will, to appoint to her estate, or to others, any or all of the principal *remaining* at the time of her death." (emphasis supplied). Thus, it is difficult to comprehend how it can be said by the majority of the Third Circuit that "the factor of fund dissolution has in no way been contemplated by the decedent."

Had the draftsman of the will stated that the wife was to receive all of the income of the trust but no less than $300 a month, the majority of the Third Circuit probably would have ruled otherwise.

When the will is further analyzed, it will be found that the reasoning of the majority of the Third Circuit errs in finding the testator's intent to take away from the widow some of her rights. The attempt to sustain the Government's position by pointing to Paragraph 11 of decedent's will (R. 10) as being "consistent with both the decedent's intent as expressed in his will and the purpose behind the marital deduction provision," (R. 52) should abort. Firstly, the mere fact that decedent recited that the monthly stipends were to be used exclusively for the spouse's sole and individual use, maintenance and support does not prevent the spouse after she receives the same from doing with it

as she pleases. The fact that decedent "endeavored to make neither liable for any debts contracted by her, nor subject to her assignment" does not evidence "a desire to limit the survivor's control over the monthly stipend." There is no doubt that once she receives the same that she can do with it as she pleases and creditors may then come in. Nextly, the Treasury's Regulations clearly state in § 20.2056(b)-5(f)(7):

> "* * * An interest passing in trust will not fail to satisfy the condition that the spouse be entitled to all the income merely because its terms provide that the right of the surviving spouse to the income shall not be subject to assignment, alienation, pledge, attachment or claims of creditors."

The use of the prescribed Treasury Department actuarial table found in Estate Tax Regulations § 20.2031-7 in the case at bar to determine the present value of the "specific portion" of the trust is feasible. Courts have used actuarial tables, such as the one employed here. These tables have been widely used for Estate Tax purposes by the Commissioner of Internal Revenue and by taxpayers.

We submit that there are not convincing reasons why the actuarial table used by the District Court and the Seventh Circuit should not be used here. It does not appear that Congress would have intended otherwise in enacting § 2056(b)(5).

I

The right in a widow to receive from a testamentary trust $300 a month out of income and corpus with the power to appoint all the remainder of the trust qualifies for the marital deduction as a "specific portion" of the trust within the meaning of Section 2056(b)(5) of the Internal Revenue Code of 1954. The provisions of Section 20.2056(b)-5 of the Treasury Regulations on Estate Tax defining "specific portion" of the entire interest in property as a fractional or percentile share of such interest are in conflict with Code Section 2056(b)(5) and therefore invalid.

The Internal Revenue Code does not define what constitutes a "specific portion" of a trust corpus, but the Treasury Regulations § 20.2056(b)-5(c) define it as a "fractional or percentile share of a property interest." This restricted definition was disapproved by the Second Circuit in *Gelb* v. *Commissioner of Internal Revenue*, 298 F. 2d 544 (2d Cir. 1962). In *Gelb* a determinable portion of the trust corpus was given to the decedent's daughter for her support and education. The surviving spouse was entitled to all of the trust income and had the sole power to appoint all of the trust corpus except the portion which would be paid to the daughter. The court held that the value of the daughter's interest could be computed actuarially and carved out of the trust corpus, thereby leaving the widow a specific portion of the trust corpus which would qualify for the marital deduction.

In the case at bar, we submit that the issue presented is the converse of that in *Gelb*. Here, the widow had a power of appointment over the entire corpus but a right to only a fixed sum each month out of income and corpus. A portion of the trust corpus, the value of which would yield a fixed sum, was carved out of the total trust corpus and the District Court and the three dissenting judges of the Third Circuit held the same

to qualify for the deduction. The majority of the Third Circuit (five judges) questioned the actuarial approach, discussed *infra,* and concluded that no method of computation could feasibly compute the amount of the specific portion.

At the outset, let us look at the history of the marital deduction.

The marital deduction was first introduced into the estate tax law as Section 361 of The Revenue Act of 1948, 62 Stat. 110, which amended Section 812(e) of the Internal Revenue Code of 1939. The legislative history of the marital deduction and its revelation of Congressional intent[1] was reviewed by this Court in *United States* v. *Stapf,* 375 U.S. 118 (1963), speaking through Mr. Justice Goldberg, where it is stated at 375 U.S. 128:

> "Our conclusion concerning the congressionally intended result under § 812(e)(1) accords with the general purpose of Congress in creating the marital deduction. The 1948 tax amendments were intended to equalize the effect of the estate taxes in community property and common-law jurisdictions. Under a community property system, such as that in Texas, the spouse receives outright ownership of one-half of the community property and only the other one-half is included in the decedent's estate. To equalize the incidence of progressively scaled estate taxes and to adhere to the patterns of state law, the marital deduction permits a deceased spouse, subject to certain requirements, to transfer free of taxes one-half of the non-community property to the surviving spouse. Although applicable to separately held property in a community property state, the primary thrust

[1] S. Rep. No. 1013, 80th Cong., 2d Sess., 1948-1 C.B. at pp. 305-306.

> of this is to extend to taxpayers in common-law States the advantages of 'estate splitting' otherwise available only in community property States. The purpose, however, is only to permit a married couple's property to be taxed in two stages and not to allow a tax-exempt transfer of wealth into succeeding generations. Thus, the marital deduction is generally restricted to the transfer of property interests that will be includible in the surviving spouse's gross estate." [2]

There is inherent in this deduction provision the expectation that the property allowed as a deduction will be taxed in the estate of the transferee upon his or her subsequent death. Thus it is sometimes said that fundamentally postponement of the tax is contemplated so that if the full marital deduction is taken, the property of the marital community will be subject to tax only once in the estate of either spouse.[3]

The Act of 1948 also provided that an interest in property passing from the decedent in trust under which the surviving spouse is entitled to all of the income for life, payable at least annually, with power in the surviving spouse to appoint the entire trust corpus, would qualify for the deduction. The Act provided further that certain interests passing to the surviving spouse which would "terminate" upon a lapse of time or the occurrence or non-occurrence of an event or contingency would not qualify for the deduction. However, the legislation failed to provide for the situation

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[2] There is no doubt in the case at bar that there will be no transfer by the surviving spouse into succeeding generations which will be tax exempt. The balance remaining in the trust estate will be includable in the surviving spouse's gross estate.

[3] *Estate of Reilly* v. *Commissioner*, 239 F. 2d 797, 799 (3d Cir. 1957) reversing and remanding 25 T.C. 366. 4 Mertens, Law of Federal Gift and Estate Taxation § 29.01.

in which the surviving spouse received an interest not in trust or received less than all of the trust income or the power to appoint less than all of the trust property. To remedy this situation, Section 2056(b)(5) of the Internal Revenue Code of 1954 was enacted and provides, in part, that a life estate with power of appointment can qualify for the marital deduction to the extent that the surviving spouse is entitled for life to all of the income from a specific portion thereof with power in the surviving spouse to appoint such specific portion.

We repeat that while the Code itself provides no definition of the term "specific portion", Section 20.2056(b)-5(c) of the Treasury Regulations defines a specific portion as a fractional or percentile share of a property interest.

The government draws heart that the regulations definition is consistent with the example of a specific portion found in the committee reports to the 1954 Code.[4]

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[4] The Congressional reports state (H. Rep. No. 1337, 83d Cong., 2d Sess., pp. 92, A319 (3 U.S.C. Cong. & Adm. News (1954) 4017, 4119, 4462; S. Rep. No. 1622, 83d Cong., 2d Sess., pp. 125, 475 (3 U.S.C. Cong. & Adm. News (1954) 4621, 4759, 5119):

> The bill makes it clear that property in a legal life estate as well as property in trust qualifies for the marital deduction and that a right to income plus a general power of appointment over only an undivided part of the property will qualify that part of the property for the marital deduction . . .
>
> . . .
>
> For example, if the decedent in his will provided for the creation of a trust under the terms of which the income from one-half of the trust property is payable to his surviving spouse with uncontrolled power in the spouse to appoint such one-half of the trust property by will, such interest will qualify as an exemption from the terminable interest rule.

Also, see S. Rep. No. 1983, 85th Cong., 2d Sess., p. 241.

The mere fact that the Congress gives an example of a fractional part of one-half does not indicate that Congress did not intend to allow the marital deduction in a case of this type when it used the term "specific portion" in Section 2056(b)(5). Also, see *Gelb*, 298 F. 2d at 551.

We realize that: "Although the weight to be given to an interpretative rule varies with its statutory and legislative context, a Treasury Regulation is particularly persuasive when, * * * it is supported by declarations of congressional intent."[5] We submit, however, that Congress did not go to the length in expressing its intent as the Treasury seems to believe it did when the Treasury adopted the fractional or percentile definition. If such was the intent of Congress, it is reasonable to suppose that it would have used such words in § 2056(b)(5) rather than the broader term "specific portion". The Second Circuit Court of Appeals in *Gelb, supra,* (factually discussed in detail, *infra*), agreed, wherein it stated at 298 F. 2d 551, "[T]hat Congress gave a fractional interest as an example of a 'specific portion' does not warrant a construction that Congress did not mean to include other instances fairly within the language and the underlying policy. We *disapprove* Regulations . . . § 20.2056(b)-5(c) insofar as it would limit a 'specific portion' to a 'fractional or percentile' share" (emphasis added). This language was subsequently adopted and referred to by the District Court in the instant case, 235 F. Supp. at 946, and by the Seventh Circuit Court of Appeals in *Citizens National Bank of Evansville* v. *United States,* 359 F. 2d at 821. The Government has filed a Petition for a

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[5] See f.n. 11, *United States* v. *Stapf,* 375 U.S. at 127.

Writ of Certiorari in *Citizens National Bank of Evansville,* No. 488.

In *Gelb,* the Second Circuit further stated, ". . . Congress spoke of a 'specific portion' not of a, 'fractional or percentile share', and nowhere indicated any policy that deductibility of a 'specific portion' should be governed by the possibility that the spouse's portion will change in value relatively more or less than the clearly nonqualifying part."[6]

The majority of the Third Circuit admits that the *Gelb* principles and disapproval of the Regulation "are appropriate to the facts of *that* case." The majority of the Third Circuit takes the position that "there is no need to take a position concerning the validity of that interpretative regulation, as it applies to this case." (R. 50)

This court speaking through Chief Justice Taney said in *United States* v. *Boisdore's Heirs,* 8 Howard 113, 122:

> "In expounding a statute, we must not be guided by a single sentence or member of a sentence, but look to the provisions of the whole law, and to its object and policy."[7]

The object and policy of the Congress in providing for the marital deduction has been well expressed by this Court in *United States* v. *Stapf, supra.*

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[6] Also see, *Allen* v. *United States,* 250 F. Supp. 155 (D.C.E.D. Mo., E.D. 1965).

[7] This was quoted with approval in *Mustro Plastics Corp.* v. *National Labor Relations Board,* 350 U.S. 270, 285 (1956), and *National Labor Relations Board* v. *Lion Oil Co., et al.,* 352 U.S. 282, 288 (1957).

II

The use of a Treasury Department actuarial table properly fixed the present value of the "specific portion" of the widow's trust as of the date of death of the testator. The attempt of the majority of the Third Circuit to read an intent of the decedent in his will which would frustrate the marital deduction is not supportable.

It should be noted that the formula used by the District Court, which was rejected by the majority of the Third Circuit is one prescribed by the Treasury Department in its Regulations on Estate Tax § 20.2031-7. The use of actuarial tables, such as the one employed, has been widely used for Estate Tax purposes by the Commissioner and by taxpayers and is a reasonable method by which one can place a present value on interests such as the one presented by this case. The extent of such use is clearly set forth in footnote 7 of the *Gelb* opinion, 298 F. 2d at 551, which reads as follows:

> The use of life expectancy tables was sanctioned by the Commissioner in the 1863 edition of "Boutwell's Manual" at p. 203, in the context of a group of regulations which, according to Carlton Fox, "appear to embody the first that were promulgated in respect of taxes on legacies." Since the federal succession tax enacted in 1862 was an inheritance tax, see Warren & Surrey, Federal Estate and Gift Taxation (1961 ed.), p. 2, it was necessary to value legacies individually, and for that purpose the 1863 regulations provided that remainders and life annuities should "be estimated by Carlisle's, or other approved tables of life annuities." As the regulations grew more elaborate, the Commissioner added examples to aid in applying the life tables "in ascertaining the values of life and reversionary interests," Instructions Concerning the Tax on Legacies, Distributive

Shares, and Successions, pp. 24-25 (Series 7-No. 3, 1878). The change to the estate tax concept in the Revenue Act of 1916, c. 463, 39 Stat. 756, and its immediate successor, the Revenue Act of 1918, c. 18, 40 Stat. 1057, was accompanied by contemporaneous acceptance of the use of life expectancy tables to value "annuities, life and remainder interests," art. 20, Regulations 37 (1919 ed.).

Introduction of the charitable deduction to the estate tax in § 403(a)(3) of the 1918 Act, 40 Stat. at 1098, led to instant acquiescence in the use of mortality tables to value charitable remainders, art. 53, Regulations 37 (1919 ed.). Perhaps their most frequent use in this area is to compute a gift to charity made subject to a life estate, see Merchants National Bank v. Commissioner, 320 U.S. 256, 259 [31 AFTR 753] fn. 6 (1943); Commissioner v. Estate of Sternberger, 348 U.S. 187, 190-192 [46 AFTR 976] (1955). The Supreme Court has even gone so far as to compel their use for such a computation when the life tenant had died before the case came to the Court, Ithaca Trust Co. v. United States, 279 U.S. 151 [7 AFTR 8856] (1929). See generally 4 Mertens, Law of Federal Gift and Estate Taxation (1959), § 28.30.

Other uses of mortality tables in Federal taxation are manifold. A typical application under the estate tax occurs if a vested remainderman dies before the life beneficiary, William Korn, 35 B. T. A. 1071 (1937). For purposes of the gift tax, they are used to value gifts of remainders, Henry F. duPont, 2 T. C. 246 (1943); Betty Dumaine, 16 T. C. 1035 (1951), and of life estates and annuities, F. J. Sensenbrenner, 46 B. T. A. 713 (1942). They have long been utilized to value annuities, not only for estate and gift tax purposes, but to allocate between return of capital and incremental return for income tax purposes. See GCM 8826, C. B. IX-2, p. 194 (1930); Florence

L. Klein, 6 B. T. A. 617 (1927); Guaranty Trust Co., 15 B. T. A. 20 (1929); Estate of Sarah A. Bergan, 1 T. C. 543 (1943). They are used also to derive the "adjusted uniform basis," the 1954 Codes' way of splitting basis between life tenant and remainderman in the event, for instance, either wishes to sell his interest while both are still alive. See Regs. § 1.1014-5(a)(1); 3A Mertens, Law of Federal Income Taxation (Zimet & Weiss rev. vol. 1958), § 21.71, at p. 200.

In *Gelb, supra,* the widow, under the residuary trust was entitled to at least $10,000.00 a year with principal to be invaded, if necessary. The widow was given the power to appoint the principal by will. The trustees (widow and son) were given the authority, in their discretion, to advance from the corpus, an amount not in excess of $5,000.00 a year for the support and education of the youngest daughter. To the Second Circuit, the specific portion could be determined after carving out the amount which could be diverted to the daughter and remanded the case to the Tax Court for actuarial calculation of the figure which could be diverted to the daughter from the corpus.[8]

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[8] The majority of the Third Circuit cites *Flesher* v. *United States,* 238 F. Supp. 119, 124 (N.D. W.Va. 1965) (f.n. 20, R. 52). However, the will of decedent Flesher provided for the son's maintenance and support in a manner consistent with his station in life. The widow was also to be provided for in a similar manner. The court in Flesher emphasized that the provisions for the widow are mentioned only secondarily. The widow-trustee had power to invade corpus for the son's maintenance and support as well as her own. Additionally, the widow did not have the power to dispose of or appoint the corpus of the trust by will because the decedent's will provided for a valid remainder over to named persons or to their heirs upon the death of the survivor of the widow or son. The power to invade for the son's benefit was not limited to a maximum figure as was done in *Gelb.*

The Second Circuit in *Gelb,* in referring to actuarial formulas, 298 F. 2d at 551, stated "the use of actuarial tables for dealing with estate tax problems has been so widespread and of such long standing that we cannot assume Congress would have balked at it here; the United States is in business with enough different taxpayers so that the law of averages has ample opportunity to work."

The majority of the Third Circuit, we submit with due respect, misreads the will of the testator (R. 7-11) in attacking the actuarial approach. Additionally, we submit that it makes other errors in its negating an actuarial approach in this case.

The Third Circuit states that the fact that the formula used is one for valuing an annuity eliminates it as appropriate for determining "specific portion." The widow was to receive a monthly stipend out of income and corpus which was in effect an "annuity" to her. To the Third Circuit, the amount invested for a widow "at age forty-two will provide the annuitant the required monthly payments for her entire life. At death, the entire fund will have been dissipated. However, the factor of fund dissolution has in no way been contemplated by the decedent" (R. 46). We do not read testator's will that he "in no way contemplated" the possibility or even probability of fund dissipation. Item 6(a) of the will (R. 8-9) clearly provides that the trustee is to pay to the wife *out of income and corpus* the allotted monthly sum "during the rest of her natural life." Additionally, the wife is given the "power, exercisable by will, to appoint to her estate, or others, any or all of the principal *remaining* at the time of her death." (em-

phasis supplied) We find it difficult to understand how it can be said by the majority of the Third Circuit that "the factor of fund dissolution has in no way been contemplated by the decedent." The opposite intent of the decedent, we maintain, is expressed when the power to appoint given to the wife by her will is of the principal *remaining* at the time of her death. This is not an artificial element as the majority of the Third Circuit would have us believe.

Further, the majority of the Third Circuit reasons that if a stipend of $350 had been capitalized that it would result in a capital value figure in excess of the value of the entire trust corpus and "theoretically a sum in excess of the entire trust corpus will qualify" (R. 47). In such a situation the marital deduction would be limited to the actual trust corpus. It would be clear that the spouse was receiving all of the income of the specific portion and some principal.

The only beneficiary named in Item 6 of the will was the wife of decedent. She is to receive a monthly stipend out of income and corpus. The balance remaining of the principal is subject to the general power of appointment conferred upon her. Thus, we submit that she is in effect the virtual owner of the trust as contemplated by Congress.[9] Factually, we submit that this case is even stronger than *Gelb* which introduced into the trust another party—the daughter who was eligible for up to $5,000.00 a year for her support and education.

[9] See S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., p. 10.

In discussing Section 812(e)(1)(F) of the 1939 Code, the Senate Finance Committee Report (S. Rep. 1013, 80th Cong., 2d Sess. Part 2, p. 16 (1948) stated:

> "These provisions have the effect of allowing a marital deduction with respect to the value of property transferred in trust by or at the direction of the decedent, where the surviving spouse, by reason of her right to the income and a power of appointment, is virtually the owner of the property. This provision is designed to allow the marital deduction for such cases where the value of the property over which the surviving spouse has a power of appointment will (if not consumed) be subject to either the estate tax or the gift tax in the case of such surviving spouse."

The fact that Item 12 of the will granted the trustee "the power to authorize payments over and above the monthly stipend up to $1,500 in the event of a serious illness or financial emergency affecting the surviving spouse" (R. 40; 50) does not work against the marital deduction. This provision is designed to take care of the widow and to permit the trustee to do so. The widow was the basic beneficiary of the trust set up in Item 6 of the will. Only after her death would others benefit and she could by will decide as to the takers. Here, too, the majority of the Third Circuit sees something in the will which should not militate against the marital deduction.

The approach taken by the majority of the Third Circuit is further weakened when it states (R. 51):

> "Thus, even if done with precision, the time of the decedent's death is the inappropriate time at which to freeze the income production status of the invested corpus for purposes of qualifying a 'specific portion' for the marital deduction."

This Court has held in *Jackson, et al.* v. *United States,* 376 U.S. 503 (1964), that qualification for the marital deduction, including a widow's allowance under state law, is determined as of the time of death. We see no reason why this ruling should not be applicable to the case at bar.[10]

The majority of the Third Circuit considers the Government's position as consistent with both the decedent's intent and the purpose behind the marital deduction provision (R. 52). It considers Item 11 of decedent's will (R. 10) as demonstrating a clear intent to "limit the survivor's control over the monthly stipend." .

This reading of the will is manifestly erroneous. The mere fact that decedent recited that the monthly stipends were to be used exclusively for the spouse's sole and individual use, maintenance and support does not prevent the spouse after she receives the money from doing with it as she pleases. The fact that decedent "endeavored to make neither liable for any debts contracted by her, nor subject to her assignment" does not evidence "a desire to limit the survivor's control over the monthly stipend." There is no doubt that when she receives the stipend that she can do with it as she pleases and her creditors at this point could come against her. Additionally, this conclusion of the majority of the Third Circuit is exactly contrary to the Treasury Regulations which state in § 20.2056(b)-5(f)(7):

> "* * * An interest passing in trust will not fail to satisfy the condition that the spouse be entitled to all the income merely because its terms provide

[10] See S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., p. 10.

that the right of the surviving spouse to the income shall not be subject to assignment, alienation, pledge, attachment or claims of creditors."

The dissenting opinion of the Third Circuit also answers the majority as follows (R. 58):

"The final point of the majority here is an attempt to extract, from paragraph 11 of the testator's will, an intent by him to 'limit the survivor's control over the monthly stipend', thus not making it akin to a fee simple.

"Paragraph 11 merely provides that the fund created for the wife is for her 'sole and separate use, maintenance and support' and not 'only that which he thought would be proper for her support and maintenance', as stated by the majority.

"As a matter of fact, this paragraph of the will has no real bearing on the issue here presented, for if the testator had provided a percentile interest for the wife, instead of a monthly stipend, this paragraph would have been equally applicable to it, so even if expressed in a percentile interest, the majority, taking the position they do here, would thus be defeating their own argument."

The majority of the Third Circuit questions the investment constant of 3½ percent (R. 48). This has been used in other estate tax situations.

In Estate of *Mary Fownes Tomec* v. *Commissioner*, 40 T.C. 134 (1963), the Tax Court determined the portion of the value of a trust created by decedent in which she retained the balance of trust income, after the payment of $2,500 income to each of her four children, to be included in the gross estate of the deceased—grantor for Federal estate tax purposes under the provisions of section 2036(a)(1) of the 1954 Code. The Tax Court

used the same method as used by the District Court in the case at bar provided in Section 20.2031-7 of the Estate Tax Regulations to carve out the portion of the trust corpus which would be excludable because of the $10,000 income payable to the children.

Mary Fownes Tomec, the decedent created an inter vivos trust providing for payment of $2,500 income to each of her four children and the balance to herself during her lifetime and upon her death the division of the corpus into trusts for the four children, or if her husband was living and at that time they were living together as husband and wife, into trusts for her children and husband. The agreement provided that in the event one of the decedent's children predeceased her leaving issue, the trustees in their absolute discretion might apply the $2,500 of such deceased child for the benefit of such deceased child's issue or any one of such issue, any such income in any year which was not paid to, or applied for the benefit of such issue during any year to be added to the principal of the trust estate. The trust provided for disposition of the trusts to be created upon the grantor's death in the event any or all of her children predeceased her and for the ultimate disposition of the trust corpus. It was held that the portion of the corpus necessary to produce $10,000 annual income is not includable in decedent's gross estate. It was also held in *Tomec,* that since the experience of the trust was less than 2 years and inadequate as a determination of the necessary portion of the corpus to support a $10,000 income that the amount of which 3½ percent is $10,000 as provided in Estate Tax Regulations, 26 C.F.R., Section 20.2031-7 should be used.

Furthermore, the 3½ percent figure was not questioned in the District Court (R. 22—footnote 4)[11] as the Government contested the right to utilize any actuarial computation.

It is of interest to note that there appears to be an inconsistency between the regulation involved in the instant case and Section 20.2056(b)-6(c) of the Treasury Regulations on Estate Tax [12] which deals with the marital deduction on life insurance payments. There is a different wording in Regulations Section 20.2056(b)-6(c) which tends to relax the application of the Code to insurance,[13] as opposed to other property, where it should be equally relaxed.

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[11] "Neither side challenges the fact that by utilizing United States Life Table 38, with interest at 3½ percent, the present worth of the right to receive $300 per month for the life of a person aged forty-two, which was the surviving spouse's age at the time of decedent's death, is $300 x 12 x 17.3911 x 1.0159 (factor for monthly payments) or $63,663.43. Of course, the government contests the right of the plaintiff to utilize any actuarial computations."

[12] § 20.2056(b)-6 *Marital deduction; life insurance or annuity payments with power of appointment in surviving spouse.*

* * *

(c) *Applicable principles.* (1) The principles set forth in paragraph (c) of § 20.2056(b)-5 for determining what constitutes a "specific portion of the entire interest" for the purpose of section 2056(b)(5) are applicable in determining what constitutes a "specific portion of all such amounts" for the purpose of section 2056(b)(6). However, the interest in the proceeds passing to the surviving spouse will not be disqualified by the fact that the installment payments or interest to which the spouse is entitled or the amount of the proceeds over which the power of appointment is exercisable may be expressed in terms of a specific sum rather than a fraction or a percentage of the proceeds provided it is shown that such sums are a definite or fixed percentage or fraction of the total proceeds.

[13] See *Estate of Reilly* v. *Commissioner*, 239 F. 2d 797 (3d Cir. 1957) reversing and remanding 25 T.C. 366.

The "variables" which the majority of the Third Circuit referred to should not be taken into consideration in the calculation of the value of the "specific portion". This is because the marital deduction is taken only once, at the death of the testator, and we can only concern ourselves with what is its value and not with what will happen. It is therefore unreasonable to assume that the method used by the District Court in calculating the specific portion is inconsistent or irreconcilable with the statutory requirement.

III

The intent of the Congress in enacting Section 2056(b)(5) in the net economic sense of providing for the marital deduction is frustrated by the holding of the majority of the Third Circuit.

In *Stapf, supra,* this Court looked to the net economic interest received by the surviving spouse and the tax effects of the construction given by the taxpayer and the majority opinion of the Court of Appeals for the Fifth Circuit. The construction given by the taxpayer was rejected by this Court since it would have permitted one-half of a spouse's wealth to pass from one generation to another without being subject either to gift or estate taxes. This result is considered squarely contrary to the concept of the marital deduction.

The marital deduction is generally restricted to the transfer of property interests that will be includable in the surviving spouse's gross estate.

Decedent's will in Item 6 provided for his widow. She was given a general power of appointment. Upon her death, the balance of the trust estate will be includable in her taxable gross estate. The majority of

the Third Circuit forgets this in its analysis. This is part of the rationale in *Stapf, supra.*

We submit that the intent of the Congress in enacting Section 2056(b)(5) of the Internal Revenue Code to provide a marital deduction is frustrated by the ruling of the majority of the Third Circuit in this case. Under its approach the estate is subject to an additional "tax bite" and upon the death of the widow the balance in the trust will also be subject to a "tax bite". Congress did not intend this whip-saw.

CONCLUSION

We submit that the decision of the Court of Appeals for the Third Circuit should be reversed.

Respectfully submitted,

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January, 1967

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248-194—67——1

CITATIONS

In the Supreme Court of the United States

OCTOBER TERM, 1966

No. 637

NORTHEASTERN PENNSYLVANIA NATIONAL BANK & TRUST COMPANY, EXECUTOR, PETITIONER

v.

UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the United States District Court for the Middle District of Pennsylvania (R. 17–27) is reported at 235 F. Supp. 941; the opinion of the court of appeals, sitting *en banc* (R. 38–59), is reported at 363 F. 2d 476.

JURISDICTION

The judgment of the court of appeals was entered on July 19, 1966 (R. 60). The petition for a writ of certiorari was filed on October 7, 1966, and was granted on December 5, 1966 (R. 61; 385 U.S. 967). This Court's jurisdiction rests on 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a bequest of property in trust providing for the monthly payment of a fixed dollar amount out of income or corpus to the decedent's widow for life constitutes a bequest of "all the income from a specific portion" of the trust property within the meaning of § 2056(b)(5) of the Internal Revenue Code of 1954 so as to qualify the bequest for a marital deduction.

STATUTES AND REGULATIONS INVOLVED

The relevant portions of §2056 of the Internal Revenue Code of 1954 and of the applicable Treasury Regulations are set forth in the Appendix, *infra* pp. 37–52. The most pertinent portion of the statute, §2056(b)(5), provides that:

> [i]n the case of an interest in property passing from the decedent, if his surviving spouse is entitled for life to all the income from the entire interest, or all the income from a specific portion thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the interest, or such specific portion, to any person other than the surviving spouse * * *

the entire interest or such specific portion thereof shall qualify for the marital deduction.

STATEMENT

Decedent died testate on May 3, 1958, survived by a widow and four children. His will devised one-half of the residue of his estate to petitioner as trustee of a spendthrift trust. The trust provided that his widow was to receive out of trust income, and corpus if necessary, the sum of $300 per month until the decedent's youngest child reached eighteen and thereafter $350 per month. In addition, the widow had the power to appoint by will the corpus of the trust to her estate or to named individuals. If the trust earned more income than was necessary to meet the monthly payments to the widow, the excess was to be accumulated. The trustee was also given discretionary power to invade up to $1,500 of corpus in the event of the widow's illness or financial emergency. The value of the trust corpus at the date of decedent's death was $69,246. (R. 5, 8–11.)

On decedent's estate tax return petitioner (his executor) reported an adjusted gross estate of $199,750, and claimed the maximum marital deduction of one-half of the adjusted gross estate ($99,875), since the value of property passing to the widow outright ($41,251) plus the value of the residuary trust ($69,246) exceeded one-half of the adjusted gross estate. The Commissioner determined that the trust did not qualify for the marital deduction. (R. 18–19.)

The question presented by this case is whether part or all of the $69,246 testamentary trust corpus qualifies for the estate tax marital deduction. This, in turn, depends on whether decedent's widow, in addi-

tion to having a general power of appointment over the trust corpus, was also entitled "for life to all the income from the entire interest, or *all the income from a specific portion* thereof, payable annually or at more frequent intervals." 1954 Code, § 2056(b)(5) (emphasis added).

On cross-motions for summary judgment, petitioner first argued that the widow was entitled to have *all* of the trust income paid to her, and thus that the full value of the trust corpus qualified for the deduction. The district court rejected this contention. Although at the time of trial the corpus had not yet produced an income in excess of $300 per month, the court found that the income from the trust could exceed that amount in which case the excess above $300 per month would be accumulated. (R. 22.) Hence, the court found that the trust did not meet the statutory requirement that *all* of the trust income be "payable [to the widow] annually or at more frequent intervals."

Petitioner next argued that the widow was entitled to have "all the income from a specific portion" of the trust corpus paid to her for life, and thus that a specific portion of the trust qualified for the deduction. The district court rejected the government's contention, based on the applicable Treasury Regulations, that none of the trust qualified because the widow was not entitled to a fractional or percentile share of the trust income. Instead, the court held that it could, through use of annuity valuation tables, value the widow's right to receive fixed payments and that this value constituted a "specific portion" of the trust corpus from which the widow

was entitled for life to "all the income." The court determined that the widow's right to payments was worth $63,663 and held decedent's estate entitled to a marital deduction in this amount. (R. 17–27).[1]

The court of appeals, sitting *en banc*, reversed, three judges dissenting, holding that it was impossible to compute any specific portion of the trust corpus from which decedent's widow is entitled for life to "all the income" generated. The court reasoned that since the rate of return on the trust assets will fluctuate over the widow's lifetime, an amount of corpus which would, in one year, produce $3,600 of income would, in other years, produce either more or less income. Therefore, no method of computation can isolate a "specific portion" of the trust corpus from which the widow will receive "all the income" actually produced, and the trust thus does not qualify for the deduction. (R. 38–59.)

SUMMARY OF ARGUMENT

In 1948, Congress enacted the marital deduction provisions of the Internal Revenue Code to equalize the effect of estate taxes in community property and common law jurisdictions. In community property jurisdictions a decedent's estate includes only one-half of the community property and his widow's

[1] The calculation was based on the annuity valuation tables contained in § 20.2031–7 of the Estate Tax Regulations. On the basis of an assumed interest yield of 3½ percent, the value of an annuity of $300 per month to decedent's widow is $63,603.43. The district court's finding of $63,663.43 is based on an erroneous stipulation by the parties regarding the calculation and does not affect the amount of tax in dispute.

estate includes the other half. In order to approximate these estate tax consequences in common law States, Congress in 1948 granted a marital deduction to the estate of a decendent in a common law jurisdiction—of up to one-half of the adjusted gross estate—for property that passes to his surviving spouse. Since the widow in a community property State is the outright owner of one-half the community property, Congress required that an interest in property bequeathed to a widow in a common law State must be the equivalent of outright ownership in order to qualify for the deduction. Thus, if the decedent bequeaths to his wife an interest less than virtual ownership, such as a life interest (with remainder to another), the bequest does not qualify for a deduction.

Recognizing, however, that bequests of property in trust were "one of the customary modes of transfer in common law states," Congress granted the deduction where the decedent established a trust for his widow and gave her (1) the right to receive all the income annually or at more frequent intervals and (2) the power to appoint the entire corpus to herself or her estate. In enacting this provision Congress noted that where the widow had these rights, she was for practical purposes the "virtual owner" of the trust property, since her income would rise and fall as the trust's income fluctuated and the value of the assets subject to the widow's power of appointment would rise and fall with the value of trust assets.

Since the 1948 legislation required the widow to receive all of the income from the entire trust if it was to qualify for the deduction, a decedent was forced to establish two trusts if he wished to leave his property in trust for the benefit of both his children and his wife. Recognizing that this requirement served no valid purpose, Congress amended the marital deduction provision in 1954 to provide that a bequest of less than all the income from a trust could qualify for the deduction if the widow received "all the income" from a "specific portion" of the trust plus a general power of appointment over either that specific portion or all of the trust assets. The legislative history confirms that this change was not intended to alter the basic requirement that if a bequest in trust is to qualify, the widow must have the rights of a virtual owner (including the right to receive all of the income from either all or a specific portion of the trust corpus).

In view of the congressional intent to grant the deduction only to interests amounting to virtual ownership and the implementing statutory requirement that "all the income" from a "specific portion" of the trust property be payable to the widow, the Treasury promulgated Regulations in 1958 providing that a partial interest in a trust's income could qualify only if the widow was receiving a fractional or percentile share of the trust income, or its equivalent. The Commissioner reasoned that only in these circumstances will the widow be the virtual owner of,

and be receiving "all the income" generated by, a "specific portion" of the trust corpus.[2]

If the widow is bequeathed one-half of the income generated by the trust corpus, it is clear that she will receive all the income from one-half of the trust assets whatever the variations in their yield. On the other hand, where the surviving spouse is given a fixed amount of income (such as $300 per month), it is impossible to determine at the time of the decedent's death any "specific portion" of trust assets from which the widow will receive "all the income" generated by those assets, for as the yield of the trust assets varies, the portion of the trust assets necessary to produce the fixed amount of income will vary. For example, if the surviving spouse were entitled to receive $4,000 per year, it would require $100,000 of trust corpus at a yield of four percent to produce the annual payment. If the yield then rose to five percent in a subsequent year, the widow would be receiving "all the income" from only $80,000 of corpus. Therefore, if the widow is bequeathed fixed payments and if, as here, the yield of the trust will vary, there is no way to isolate any specific portion of the trust corpus from which she will (like a "virtual owner" of a specific portion of the trust property) receive all the income actually generated, as the statute requires. Accordingly, the Regulations, in requiring that the widow's

[2] Other language in § 2056(b)(5) and the Regulations thereunder allows a deduction where the widow is given all the income from, and a general power of appointment over, a specific item of trust property (such as a piece of commercial realty).

income interest be cast in terms of a fractional share or its equivalent, manifestly carry out Congress' intent that the widow must be the "virtual owner" of a "specific portion" of the trust property in order for a marital deduction to be allowable.

Some lower courts have disapproved the Regulations on the ground that although, as here, the income and value of the trust's assets will fluctuate, the value of the widow's right to receive fixed payments can be computed and this value can be considered a specific portion of the trust corpus. Aside from the fact that the two methods of valuation which have been used—one based on an annuity and the other on a capitalization computation—produce markedly different results, treating an artificially computed value as a "specific portion" of trust assets is improper for two basic reasons. First, it assumes that whether a bequest in trust qualifies for the marital deduction turns solely on whether it can be valued. Under § 2056(b), however, a bequest can qualify only if it has the characteristics of virtual ownership required by the statute, *i.e.,* only if the widow will actually receive "all the income" generated by a specific portion of the corpus. Second, these computational techniques are based on various artificial assumptions, including the assumption that the corpus will have an unvarying yield of 3½ percent. Because these computations assume—contrary to fact—that the trust will earn a fixed constant yield, they cannot serve to isolate as of the date of decedent's death (when qualification for the deduction must be determined) a specific portion of variable yield trust assets from which the widow will receive all the income actually pro-

duced. To permit a deduction because a widow's right to receive fixed periodic payments can be valued by arbitrarily assuming a constant hypothetical yield would effectively read out of the statute the explicit requirement that the widow receive "all the income from a specific portion" of the trust assets.

When, as here, the value and income of the trust assets can vary, only an interest in trust income expressed as a fractional share or its equivalent, together with a power of appointment over such share of the corpus, can isolate a specific portion of the trust from which the widow is entitled to "all the income" and over which she has the power of disposition, as the statute requires. The Regulations should therefore be upheld.

ARGUMENT

I

IN ORDER TO EQUALIZE THE ESTATE TAX BURDEN IN COMMON LAW AND COMMUNITY PROPERTY STATES, CONGRESS GRANTED A MARITAL DEDUCTION TO A DECEDENT IN A COMMON LAW STATE WHO MADE HIS WIDOW THE "VIRTUAL OWNER" OF PROPERTY HELD IN TRUST

Congress first enacted the marital deduction provision in 1948 [3] in order "to equalize the effect of the estate taxes in community property and common-law jurisdictions." *United States* v. *Stapf,* 375 U.S. 118, 128; see also *Jackson* v. *United States,* 376 U.S. 503, 510. Under a community property system, a married

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[3] Section 361 of the Revenue Act of 1948, c. 168, 62 Stat. 117, amending § 812 of the Internal Revenue Code of 1939.

person owns—and thus his estate includes—only one-half of the community property, the other half belonging to his surviving spouse. In order to approximate this result in common law States, Congress granted a marital deduction—of up to one-half of the adjusted gross estate—for property that passes from the decedent to his surviving spouse. Since in community property States the widow owns one-half of the community property outright,[4] Congress required that the interest passing from a decedent to his widow in a common law State must be equivalent to absolute ownership, if it is to qualify for the marital deduction.[5]

Consistent with its objective of equalizing the tax treatment of residents of common law and community property States, Congress refused to allow any marital deduction where the decedent gave his wife substantially less rights than she would have had in community property. For example, if decedent gave his wife only a life interest, or if her interest would terminate upon remarriage, and the remainder then pass to someone else, the bequest would not qualify for the deduction. (See § 2056 (b)(1) (App. *infra*, p. 37), denying any marital deduction where a decedent bequeaths a "terminable interest" to his widow.)

Congress, however, recognized that bequests of

[4] *E.g.*, Arizona Revised Statutes, § 14-203; California Probate Code, § 201; Louisiana Civil Code, Article 2406; Texas Probate Code, § 45.

[5] Community property, of course, does not qualify for the marital deduction. § 2056(c)(2). (Unless otherwise indicated references are to the 1954 Code.)

property in trust were "one of the customary mode of transfer of property in common-law States"[6] and thus in the original 1948 legislation it specifically granted a marital deduction where the decedent creates a trust and the "surviving spouse is entitled for life to *all the income* from the corpus of the trust, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire corpus" to herself or her estate.[7] In such a case, since the widow was entitled to receive currently "all the income" from the trust, she would receive the benefit or burden of any increase or decrease in the trust's income. Similarly, since she had the power "to appoint the entire corpus" to herself or her estate, any increase or decrease in the value of the trust assets would be directly reflected in the amount of property over which she had a power of disposition. In these two important respects she was in exactly the same position as if she had owned the property outright. Congress decided that, where she had these key incidents of ownership, the estate should be entitled to the marital deduction because the surviving widow was for practical purposes "the virtual owner of the property." S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess., p. 16 (1948-1 Cum. Bull. 331, 342).

Thus, under the original 1948 legislation creating the marital deduction, if a decedent left one-half of

[6] S. Rep. No. 1013, 80th Cong., 2d Sess., p. 28 (1948-1 Cum. Bull. 285, 305).

[7] 1939 Code, § 812(e)(1)(F), as added by § 361 of the Revenue Act of 1948, c. 168, 62 Stat. 117 (emphasis added).

his property in one trust for the exclusive benefit of his widow—giving her all the income from this trust and a general power of appointment over the corpus—and the other one-half of his property in another trust for his children, he was entitled to a marital deduction with respect to the first trust. If a decedent left all of his property in a single trust, however, giving his widow one half of the income and a general power of appointment over one-half of the corpus, his estate would not be entitled to any marital deduction, because his widow neither received "all the income from the corpus of the trust" nor had a general power "to appoint the entire corpus."[8] This result followed even though the widow's rights would be substantially the same as if the decedent had created two trusts—she would receive one-half of the income from his estate and have a general power of appointment over one-half of his estate. In either event, her income would rise and fall as the income from the trust increased or decreased, and the amount of property over which she had a power of disposition would fluctuate as the value of the trust assets increased or decreased.

Recognizing that there was no good reason to require a decedent to create two separate trusts, Congress in 1954 revised the marital deduction provision

[8] See *Estate of Shedd* v. *Commissioner*, 237 F. 2d 345 (C.A. 9), certiorari denied, 352 U.S. 1024; *Estate of Sweet* v. *Commissioner*, 234 F. 2d 401 (C.A. 10), certiorari denied, 352 U.S. 878; *Estate of Hoffenberg* v. *Commissioner*, 22 T.C. 1185, affirmed, 223 F. 2d 470 (C.A. 2); *Estate of Stallworth* v. *Commissioner*, 260 F. 2d 760 (C.A. 5); Cf. *Estate of Joseph A. Barry, Sr.* v. *Commissioner* (decided April 27, 1956) 15 T.C.M. 502.

to allow such deduction where the decedent gave his widow "all the income from the entire interest, or *all the income from a specific portion thereof*" plus a general power "to appoint the entire interest, or such specific portion." 1954 Code, § 2056(b)(5) (emphasis supplied).[9] This statutory change removed the necessity for creating two separate trusts; it did not, however, relax the requirement that the widow must be "the virtual owner of the property," *i.e.*, that the amount of her income and the amount of property covered by her power of appointment must depend directly on the trust's actual income and the value of its assets. By this revision Congress intended to allow a marital deduction if the widow became the virtual owner of "an undivided part of the [trust] property." H. Rep. No. 1337, 83d Cong., 2d Sess., p. 92; S. Rep. No. 1622, 83d Cong., 2d Sess., p. 125. The Committee Reports give this example: "[I]f the decedent in his will provided for the creation of a trust under the terms of which the income from one-half of the trust property is payable to this surviving spouse with uncontrolled power in the spouse to appoint such one-half of the trust property by will, such interest will qualify as an exception for the terminable interest rule." H. Rep. No. 1337, 83d Cong., 2d Sess., p. A319; S. Rep. No. 1622, 83d Cong., 2d Sess., p. 475.

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[9] Congress in 1958 made this 1954 amendment retroactive to the original enactment of the marital deduction provision in 1948. Technical Amendments Act of 1958, § 93, P.L. 85-866, 72 Stat. 1668.

II

THE REGULATIONS RECOGNIZE, AS DID CONGRESS, THAT A WIDOW IS NOT THE "VIRTUAL OWNER" OF PROPERTY UNLESS (LIKE A WIDOW IN A COMMUNITY PROPERTY STATE) HER INCOME RISES AND FALLS WITH THE TRUST'S INCOME, AND THUS THAT NO DEDUCTION IS ALLOWABLE WHERE THE WIDOW IS MERELY ENTITLED TO FIXED PAYMENTS OF INCOME

In order to implement the Congressional objective of permitting a marital deduction where the widow's partial interest in the trust corpus amounts to virtual ownership, the Treasury promulgated Regulations [10] providing that the widow is entitled to "all the income from a specific portion" of a trust only if she receives a "fractional or percentile share" of the trust income or its "equivalent," since only an interest of this

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[10] § 20.2056(b)–5(c) of Treasury Regulations (1954 Code) reads in part as follows:

"A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse in income and as to the power constitute a fractional or percentile share of a property interest so that such interest or share in the surviving spouse reflects its proportionate share of the increment or decline in the whole of the property interest to which the income rights and the power relate. Thus, if the right of the spouse to income and the power extend to one-half or a specified percentage of the property, or the equivalent, the interest is considered as a specific portion. On the other hand, if the annual income of the spouse is limited to a specific sum, or if she has a power to appoint only a specific sum out of a larger fund, the interest is not a deductible interest. Even though the rights in the surviving spouse may not be expressed in terms of a definite fraction or percentage, a deduction may be allowable if it is shown

kind carries with it a participation in income fluctuations that is a hallmark of property ownership.[11]

If the surviving spouse is given all the income from, and a general power of appointment over, one-half of the trust corpus, the precise portion of the corpus from which she will receive all the income actually produced during her lifetime and over which she will have a powe. of disposition can be readily isolated. This portion will qualify for the deduction because thenceforth the widow will participate in income and value fluctuations as an owner would. Where, however, as in the instant case, the widow is given the right to receive only a fixed monthly payment from a trust with variable income, she will not receive "all the income from a specific portion" of the trust because, as the trust's income varies, the amount of trust assets required to produce the fixed monthly income will also vary. For example, if a testamentary trust provided that the surviving spouse was to receive $4,000 annually, it would require $100,000 of

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that the effect of local law is to give the spouse rights which are identical to those she would have acquired if the size of the share had been expressed in terms of a definite fraction or percentage."

[11] Similarly, it is also clear that if the trust corpus includes a specific item of property (*e.g.*, a commercial building or a block of AT&T shares), the widow is to receive all of the income generated by this property, and she also has a general power of appointment over the specific item of property, the bequest will qualify for the deduction, since the widow is entitled to all of the income from and a power of appointment over the entire interest in the particular item of property. Treasury Regulations (1954 Code), § 20.2056(b)-5(d) (App. infra, p. 44). Prior to the 1954 version, such a bequest would not have qualified for a deduction. 1939 Code, § 812(e)(1)(F).

trust assets at an assumed four percent yield to produce the necessary income. If the yield should rise the following year to five percent, the widow would be receiving the income generated by only $80,000 of trust assets. Thus, had the value of the marital deduction been computed on the basis of an assumed four percent yield, an increase in the yield would mean that the widow was not receiving for her life all the income from a part of the $100,000 of corpus which had qualified for the marital deduction.

The Regulations recognize, however, that qualification for the deduction does not necessarily turn upon using the terminology of fractional or percentile interest; all that is required is that the interest be the "equivalent" of a fractional share. The Regulations give the example of a widow who was given the income from, and a power of appointment over, 100 out of 250 shares of stock held in trust, and explains that her interest would qualify for the deduction if she was entitled under local law to share proportionately in stock splits, stock dividends, distributions of capital, etc., for in that event she would be the virtual owner of those 100 shares, *i.e.*, her income would fluctuate as the income of the 100 shares rose and fell and the value of the property she could appoint would fluctuate with the value of the 100 shares.

Another example of a bequest that is "equivalent" to a fractional share is a devise of a fixed amount of income from a trust whose income cannot vary. For example, if a testator established a trust of fixed-yield assets, such as government bonds or notes, with a

face value of $100,000 and a yield of $4,000 a year, and provided that his spouse was to receive $2,000 per year with the testamentary power to appoint all of the trust, it would be clear that the widow would, under these limited circumstances, be receiving all of the actual income from $50,000 (*i.e.,* the equivalent of one-half) of the corpus and that amount would qualify for the deduction.[12]

Closely paralleling Code § 2056(b)(5) is § 2056(b)(6) which grants a marital deduction when proceeds of a life insurance, endowment or annuity contract are to be retained by the insurance company, which agrees to pay interest on the principal amount of the policy (or a portion thereof) to the widow during her life at a fixed rate and she has a general power to appoint the principal amount (or a portion thereof) at her death.[13] This section also utilizes the "specific portion" concept, and, contrary to the petitioner's suggestion (Br. 25), does not relax the requirement that the widow have a fractional share or its equivalent. In virtually all cases where insurance proceeds are left with the insurer, the insurance contract provides for the payment to the beneficiary of a fixed monthly sum computed on the basis of a fixed yield. Assume, for example, that the decendent left the

[12] We are assuming that the trustee cannot alter the corpus of the trust and that at the maturity date of the notes, the trust will terminate and the corpus will be paid to the widow. In such a case, the income of the trust will not vary.

[13] One variation is for the insurer to agree to pay the widow periodic installments for her life consisting of both interest at a fixed rate and principal and for her to have a general power to appoint the principal remaining at her death.

proceeds of a $100,000 insurance policy with the company, which was obligated to pay the widow $4,000 a year (as interest) during her life and, at her death, to pay the $100,000 principal amount as she designated. The effect of such an arrangement is to impose upon the insurance company, as a debtor, the obligation to make fixed interest payments as compensation for the use of the money during the widow's life. In that situation the widow, unlike the beneficiary of a variable yield trust, has no interest in, or right to, any undivided portion of the total income or assets of the insurance company; her only right is to received fixed interest payments during her life and to appoint the principal amount. Thus, if, in the example above, the widow had the right to $2,000 of the annual interest payments and the right to appoint $50,000 at her death, she in fact will receive a "specific portion" (one half) of "all" the income which the insurance company is obligated to pay the decendent's beneficiaries, as well as the right to appoint a "specific portion" (one half) of the entire proceeds. For neither the amount of such income nor the value of what she can appoint at her death can vary during her life. Thus, the Regulations provide:

> The principles set forth in Paragraph (c) of § 20.2056(b)-5 for determining what constitutes a "specific portion of the entire interest" for the purpose of section 2056(b)(5) are applicable in determining what constitutes a "specific portion of all such amounts" for the purpose of section 2056(b)(6). However, the interest in the proceeds passing to the surviving spouse will not be disqualified by the fact that the installment payments or interest to which

> the spouse is entitled or the amount of the proceeds over which the power of appointment is exercisable may be expressed in terms of a specific sum rather than a fraction or a percentage of the proceeds *provided* it is shown that such sums are a definite or *fixed percentage* or *fraction* of the total proceeds. [Emphasis supplied.][14]

Thus the consistent pattern of the marital deduction Regulations is to require that the widow receive a fractional or percentile share of the income produced by the underlying property or the equivalent thereof.[15] Unless the widow receives such an interest, it is impossible to identify a "specific portion" of the corpus from which she will receive "all the income" generated, as the statute requires and as an owner of such portion would. There can be no doubt that these Regulations carry out Congress' intent in enacting § 2056(b)(5) and (6), and they should therefore be upheld. See *Commissioner* v. *South Texas Co.*, 333 U.S. 496, 501; *Fawcus Machine Co.* v. *United States*, 282 U.S. 375, 378. As a contemporaneous construction of the statute by those who were charged with "setting [the] machinery in motion," the Regulations are entitled to "peculiar weight." *Norwegian Nitrogen Products Co.* v. *United States*, 288 U.S. 294, 315. This is especially true when the subject matter is technical and complex and the interpretation is supported by a specific example in the committee re-

[14] Treas. Regs. § 20.2056(b)-6(c).

[15] Or, as discussed *supra* fn. 11, p. 16, all of the income generated by a specific item of property.

ports accompanying the statute. See *Helvering* v. *Wilshire Oil Co.*, 308 U.S. 90, 102; *United States* v. *Stapf*, 375 U.S. 118, 126, 127, fn. 11.[16]

[16] Our interpretation of the Regulations is also supported by subsequent congressional action. On September 2, 1958, Congress amended § 812(e)(1)(F) of the 1939 Code in order to make the 1954 revision (which added the language here in dispute) retroactive to the original enactment of the marital deduction provision in 1948. Technical Amendments Act of 1958, § 93, P.L. 85-866, 72 Stat. 1668. Since the Regulations here in question had first been proposed on October 16, 1956 (21 Fed. Register, part 7, pp. 7850, 7917), and finally adopted on June 16, 1958 (23 Fed. Register, part 4, p. 4529; see also T.D. 6296, 1958-2 Cum. Bull. 432, 572, 624), the Treasury's interpretation of the statutory phrase "all the income from a specific portion" had been known for almost two years prior to the 1958 amendment. If Congress had been dissatisfied with this interpretation, one would expect it to have so indicated at the time it retroactively amended the 1939 Code. Instead, it used the same language in the committee reports accompanying the 1958 amendment (including a specific example of a fractional share) that it used in the committee reports accompanying the 1954 legislation. S. Rep. 1983, 85th Cong., 2d Sess., pp. 107, 241. Moreover, the Treasury has consistently adhered to this interpretation of § 2056(b)(5) for more than ten years.

III

WHERE A WIDOW IS ENTITLED TO A FIXED AMOUNT OF INCOME FROM A TRUST WITH A VARIABLE INCOME, THERE IS NO METHOD FOR ISOLATING ANY "SPECIFIC PORTION" OF THE TRUST ASSETS FROM WHICH SHE IS ENTITLED TO "ALL THE INCOME" ACTUALLY GENERATED, AS REQUIRED BY § 2056(b)(5).

Some courts have disapproved the Regulations on the ground that although, as is true here, the trust income will vary, fixed payments bequeathed to the widow can be valued. Since they can be valued, these courts have reasoned that such value can be considered a "specific portion" under §2056(b)(5). This approach is also reflected in petitioner's contention that "because the marital deduction is taken only once, at the death of the testator, * * * we can only concern ourselves with what is its value and not with what will happen." (Br. 26.)

The basic flaw in this analysis is its assumption that valuation is the touchstone for qualification, so that any income interest plus power of appointment will qualify for the deduction, when, in fact, the gift to the widow can qualify only if it has the characteristics of virtual ownership required by the statute. If the interest does qualify, valuation is, of course, necessary since the deduction is limited to that amount. The question here, however, is whether—under the tests of §2056(b), which are designed to implement the requirement that the widow receive an interest amounting to virtual ownership—the interest qualifies for the marital deduction at all, whatever its value may be.

It is clear that § 2056(b) requires an examination of what may actually happen after decedent's death in order to determine whether the interest is a nondeductible terminable interest. For example, if the interest given to the widow may terminate at or before her death and the property pass to another, it does not qualify, although it can be valued. See § 2056(b) (1) and (2). Turning to the instant case, it is apparent that the actual income of the trust will fluctuate—perhaps markedly—during the widow's lifetime, but that, regardless of whether the income rises well above or falls substantially below $3,600 per year, the widow's income will remain constant. Therefore, she will not receive "all the income" generated by the trust or by any "specific portion" of the trust, and she does not have an interest equivalent to "virtual ownership" of any specific portion of the assets. As the court below held, where, as in the present case, the trust income is variable and the widow is entitled to fixed payments, no computational technique can isolate or identify a specific portion of the corpus from which she will receive all the income generated.

The two lower courts which have rejected the government's argument have used two markedly different computational methods in an effort to value the widow's rights to fixed payments.[17] Under one such method—the annuity approach—the court computes the amount of corpus that is necessary in order to

[17] The district court in the instant case and the Seventh Circuit in *Citizens National Bank of Evansville* v. *United States*, 359 F. 2d 817, government's petition for certiorari pending, No. 488, this Term.

make the fixed periodic payments (*e.g.,* $300 per month) throughout the widow's life expectancy, using both income earned at an arbitrarily assumed yield and corpus to make the payments, so that at the end of the period the corpus will theoretically be exhausted. Under the other method—the capitalization approach—the court computes the amount of corpus that is necessary in order to earn—at an arbitrarily assumed yield—an amount of income equal to the fixed periodic payments, so that the corpus will theoretically never be exhausted or diminished. The results of these two methods are strikingly different.

In this case, for example, the district court used the annuity method, employing the annuity valuation tables contained in §20.2031–7 of the Estate Tax Regulations to compute the value of the widow's rights.[18] Although this Regulation is extremely useful in resolving the difficult valuation problems which exist when an annuity is includible in an estate, it is, as the court below concluded, totally inappropriate for determining a specific portion of the trust from which all of the income is payable to the widow.

Although the statute clearly requires as a prerequisite to deductibility that the widow have the right to receive all the income actually produced by a specific portion of the trust assets for her actual lifetime so that her interest really is the equivalent of ownership, the annuity tables assume a constant yield of 3½ percent, an actuarially determined life expectancy for the widow, and exhaustion of the corpus over that

[18] See fn. 1, *supra*, p. 5.

period. Such assumptions must, of necessity, be made when it is necessary to value an annuity, but they should not be used here, since Congress has granted a marital deduction only if the decedent's will has actually given his widow the right to receive for her life all of the income actually generated by some specific portion of the trust assets. Furthermore, introducing the factor of actuarially determined life expectancy means that the size of the marital deduction will depend upon the widow's age—the younger the widow, the larger the estate's marital deduction will be—a result for which the statute provides no inkling of support. Finally, since §2056(b)(1)(C) specifically provides that a direction in a decedent's will that his executor or trustee use a bequest of funds to purchase an annuity for his wife disqualifies the bequest for the marital deduction, it is anomalous to compute the "specific portion" as if that were just what the trustee had been directed to do.

The other computational method—the capitalization approach, which was approved of by the Seventh Circuit in *Citizens National Bank of Evansville* v. *United States,* 359 F. 2d 817, government's petition for a writ of certiorari pending, No. 488, this Term—is equally unsatisfactory. The facts in *Citizens National Bank* are substantially the same as in the instant case. The decedent had created a residuary testamentary trust worth $123,000, which provided that his widow was to receive $200 per month for the first five years after his death, and thereafter all of the income from the trust, with power to appoint all

of the trust property at her death. The court of appeals upheld the district court's determination that $68,572 of the trust qualified for the marital deduction since that was the capitalized amount of corpus necessary to produce an income of $200 per month assuming a 3½ percent annual yield (*i.e.*, $68,572 × 3½ percent = $2,400 per year). Although the capitalization approach does not involve artificial assumptions with respect to corpus dissipation and the widow's life expectancy (which are required by the annuity method), the capitalization technique is, nevertheless, no more appropriate than the annuity approach for isolating a specific portion of variable yield assets from which the widow is entitled to receive all the actual income. For the capitalization technique, like the annuity method used by the district court in the instant case, arbitrarily assumes that the trust assets will produce a fixed annual yield (*e.g.*, 3½ percent in the *Citizens Bank* case), which will remain constant over the widow's lifetime. Both of these assumptions are almost sure to be contrary to the actual facts. In any year in which the yield is greater than 3½ percent, the widow will not receive all the income generated by the $68,572 of corpus for which the deduction was granted.[19]

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[19] *Tomec* v. *Commissioner*, 40 T.C. 134, heavily relied upon by petitioner (Br. 23–24), deals with the question of the proper valuation of property includible in the decedent's gross estate under § 2036 because she had retained a partial life interest therein. The question here presented is not the value of the widow's right to fixed payments but whether she was given all the income generated by a specific portion of the trust assets. **(Cont'd)**

The defects inherent in these computational methods are highlighted by the markedly diverse results they produce. If a decedent dies leaving a $300,000 trust from which his widow is to receive $300 a month, the capitalization method adopted by the Seventh Circuit in *Citizens National Bank* would produce a specific portion of $102,806, and the actuarial method used by the district court in this case would produce a marital deduction of $64,706 if the widow were 40 years old, and a deduction of $40,813 if she were 60 years old.

IV

PETITIONER'S ARGUMENTS TO THE CONTRARY ARE WITHOUT MERIT

1. In arguing that the Regulations are invalid, petitioner relies on *Gelb* v. *Commissioner*, 298 F. 2d 544 (C.A. 2). In *Gelb*, the decedent had established a residuary testamentary trust in which his widow was entitled to all the income for her life with a general power of appointment over the corpus. The will also gave the trustees discretionary power to invade corpus up to $5,000 per year for the support, maintenance and education of the decedent's youngest daughter. Since the widow was entitled to all of the income from the entire trust, the bequest met the § 2056(b)(5) requirement regarding income. The Commissioner contended, however, that the widow did not possess the requisite power of appointment be-

Use of an assumed yield of 3½ percent to solve valuation problems under § 2036 in no way justifies computing a specific portion under § 2056(b)(5) on the basis of an assumed rather than the actual income of the corpus.

cause the trustees' power to invade corpus in favor of the youngest daughter meant that the widow did not have the power to appoint either the entire corpus or a specific portion thereof. The Second Circuit held that, because of the trustees' power to invade corpus, the widow did not have a power of appointment over the entire trust, but that she did have a power of appointment over a specific portion of the corpus which could be computed by subtracting from the full value of the trust corpus the maximum amount of corpus which the trustees could reasonably be expected to pay to or for the daughter. The court disapproved Regulation 105, § 81.47(a)(c)(3) (now Regulation § 20.2056(b)-5(c)), to the extent that "it would limit a 'specific portion' to 'a fractional or percentile share.'" 298 F. 2d at 551.

As the Third Circuit noted in the instant case, *Gelb* is distinguishable from this case because the question in *Gelb* was whether there was an identifiable minimum portion of the corpus over which the widow had a power of appointment. The maximum amount which could be withdrawn annually for the daughter in *Gelb* was $5,000. Multiplying this figure by the sole variable—the life expectancies of the widow and daughter—produced the maximum amount which could be expected to be diverted to the daughter and, conversely, the minimum amount which the widow could reasonably be expected to have the power to appoint. There was no question in *Gelb* as to whether the widow had the requisite right to income,

since she was entitled to receive all the income produced by the trust.

In the instant case, however, the widow has the right to receive fixed income payments from a trust with fluctuating income. It is thus impossible to compute even a minimum specific portion of trust corpus, all of the income from which is payable to the widow, because each computation depends upon an arbitrary assumption as to the yield of the trust assets, and there is no way of knowing in advance the actual income yield of trust assets, unless the trust is restricted to owning solely fixed-yield assets. Therefore, even if the *Gelb* result is accepted, it does not control the question presented by this case.

Although it is thus distinguishable, we believe that *Gelb* was wrongly decided for two reasons. First, like the reasoning of the district court in this case and the Seventh Circuit in *Citizens National Bank, Gelb* is based on the fallacious assumption that if the widow's interest can be valued, that value will qualify for the marital deduction. As discussed, *supra*, p. 22, quite the contrary is true. Whatever the value of the interest bequeathed to the widow, it can qualify for the marital deduction only if it has the characteristics of virtual ownership required by the statute.

Second, the court erroneously assumed that if the widow had a power of appointment over a fixed dollar amount of corpus, that figure could be considered a "specific portion" and would, therefore, qualify for

the deduction.[20] However, when, as in *Gelb*, the corpus can fluctuate in value, the power to appoint a fixed dollar amount of corpus is not the equivalent of virtual ownership of a specific portion of trust assets, since the surviving spouse does not share in fluctuations in the value of the trust assets. Furthermore, the approach of the *Gelb* court would give residents of common law jurisdictions a significant advantage over residents of community property States.

Assume, for example, that a husband in a common-law State left his entire estate worth $200,000 in trust and gave his widow all of the trust income for her life plus a testamentary general power to appoint $100,000 of corpus (the remaining corpus being payable to the children). Assume also that before the widow's death, the trust corpus increased in value from $200,000 to $600,000 and that the widow exercised her power of appointment in favor of the children. In such a case, the *Gelb* court's approach would allow the husband's estate a $100,000 marital deduction with the result that only $100,000 is included in the husband's estate and $100,000 in his widow's estate (*i.e.*, the maximum amount of assets subject to her general power of appointment). Thus, $600,000 would pass to the children but only $200,000 would have been subject to an estate tax.

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[20] See *Allen* v. *United States*, 250 F. Supp. 155, 157 (E.D. Mo.); cf. *Flesher* v. *United States*, 238 F. Supp. 119, 124 (N.D. W. Va.).

However, if the same situation had arisen in a community property State, decedent and his wife would each have owned one-half the property outright. Thus, if the husband died and bequeathed his one-half interest in the community property in trust, the income payable to his wife for life, remainder to his children, his estate would, like the estate of the common law resident, include $100,000. When his wife dies leaving her one-half interest in the community property to her children, her estate will include one-half the value of the property at the time of her death—$300,000. Since the widow in a community property State has outright ownership of one-half the community property, she is taxable on one half of its appreciated value.

The result in both cases is that $600,000 passes to the children, but in a community property State $400,000 is subject to tax, while, if the *Gelb* rationale is accepted, only $200,000 would be subject to tax in a common law State. Thus, although the congressional purpose in enacting the marital deduction was to give estates in common law jurisdictions comparable tax treatment to those in community property States, the effect of the *Gelb* rule is to give them more favorable treatment. This discrepancy would be avoided if a decendent in a common law State, in order to obtain a marital deduction, were required to give his widow a fractional share of the corpus (in this case one-half), for then the value of the assets subject to her power of appointment would rise with the value of the trust as-

sets, so that the appreciated value of the assets subject to her power would be included in her estate.[21]

Therefore, the Regulations here in question correctly implement congressional intent when they require, in order for a deduction to be allowed, that the bequest to the widow must be a fractional share or its equivalent, so that the widow's income rises and falls as the trust's income fluctuates and the value of the assets subject to her power of appointment rises and falls as the value of the trust assets fluctuates, *i.e.*, the Regulations correctly require the widow in a com-

[21] It is clear that comparability in estate tax consequences between common law and community property jurisdictions can be achieved only by requiring that a specific portion be cast in terms of a fractional interest or its equivalent. Using the examples stated in the text, in which the property passing to the children was worth \$200,000 at the death of the husband and \$600,000 at the death of the widow, the estate tax results may be summarized as follows:

Results under—	Amount subject to tax on husband's death	Amount subject to tax on widow's death
Community property State	\$100,000	\$300,000
Common law State—fracional share	100,000	300,000
Common law State—*Gelb* rule	100,000	100,000

Moreover, if the value of the property passing to the children *decreased* from \$200,000 at the husband's death to \$100,000 at the widow's death, comparability again is achieved only by requiring the widow to receive a fractional interest:

Results under—	Amount subject to tax on husband's death	Amount subject to tax on widow's death
Community property State	\$100,000	\$50,000
Common law State—fractional share	100,000	50,000
Common law State—*Gelb* rule	100,000	100,000

mon law State to be the "virtual owner" of a specific portion of the trust assets as the widow in a community property State would be.

2. Petitioner also argues that since the widow in the instant case is the trust's only beneficiary, she must be "the virtual owner of the trust as contemplated by Congress" (Br. 20). Congress has, however, set forth the attributes of virtual ownership, all of which must be present in order for the trust to qualify. One of those attributes is that the income must be payable to the widow "annually or at more frequent intervals." § 2056(b)(5). Thus, if a trust instrument (1) provides that the income is to be accumulated for ten years, that the accumulated income is then to be paid to the widow, and that the income is thereafter to be paid to her currently, and (2) grants the widow a testamentary general power of appointment over the corpus, the trust clearly does not qualify for the marital deduction, even though the widow is the only beneficiary of the trust. In this case, the district court found that the trust could earn income in excess of that required to meet the $300 monthly payments to the widow and that such excess would be accumulated (R. 22). In these circumstances, the trust cannot qualify for the deduction even though the widow will either ultimately receive or have a power of appointment over all the income.

3. Finally, petitioner argues that so long as the property will be included in the estate of the widow at her death and subjected to taxation at that time, the trust should qualify for the deduction. (Br. 12, 26–27.) If Congress had intended to grant a marital

deduction whenever assets in trust would be included in the widow's gross estate, then § 2056(b)(5) would have provided such a deduction whenever the decedent established a trust and gave his widow only a general power of appointment over the corpus. (§ 2041 provides that property subject to a person's general power of appointment will be included in the power holder's estate.) However, § 2056(b)(5) grants a marital deduction for trust assets only when the decedent has given his surviving spouse both a general power of appointment and the requisite income interest so that she will be the virtual owner of the property, like the widow in a community property State. As this Court stated in *Jackson* v. *United States, supra,* p. 510, "the determinative factor [as to deductibility] is not taxability to the surviving spouse but terminability as defined by the statute."

In summary, it may be appealing to use some computational technique based on arbitrary assumptions as to yield, life expectancies, etc., in order to estimate the value of a widow's right to receive fixed payments out of income or corpus and then to use this estimate as a "specific portion" of the corpus that will qualify for the deduction. However, such attempts fly squarely in the face of the Code requirement that the surviving spouse actually receive all the income of a specific portion—a requirement compelled by the congressional purpose of achieving uniform federal estate tax consequences in common law and community property States by insuring that only an in-

terest equivalent to outright ownership should qualify for the marital deduction.

Indeed, petitioner's argument would in effect write out of the statute the requirement that the surviving spouse must receive "all the income" from at least a "specific portion" of the property. For it always is possible, by using arbitrarily assumed yields or life expectancies, to calculate that portion of the property which, on the basis of such assumptions, will produce the designated dollar payments. But Congress could not have intended the courts to interpret the statutory phrase "all the income from a specific portion" so as to deprive it of any meaningful content. On the contrary, the correct interpretation of the statute is that contained in the Regulations—that "specific portion" means a fractional or percentile interest or its equivalent, and not an arbitrarily computed amount whose sole justification is that it will theoretically produce periodic income equal to the fixed payments required by the will.

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be affirmed.

Respectfully submitted.

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MARCH 1967.

APPENDIX

Internal Revenue Code of 1954 (26 U.S.C., 1958 ed.):

SEC. 2056. BEQUESTS, ETC., TO SURVIVING SPOUSE.

(a) *Allowance of Marital Deduction.*—For purposes of the tax imposed by section 2001, the value of the taxable estate shall, except as limited by subsections (b), (c), and (d), be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

(b) *Limitation in the Case of Life Estate or Other Terminable Interest.*—

(1) *General rule.*—Where, on the lapse of time, on the occurrence of an event or contingency, or on the failure of an event or contingency to occur, an interest passing to the surviving spouse will terminate or fail, no deduction shall be allowed under this section with respect to such interest—

(A) if an interest in such property passes or has passed (for less than an adequate and full consideration in money or money's worth) from the decedent to any person other than such surviving spouse (or the estate of such spouse); and

(B) if by reason of such passing such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest so passing to the surviving spouse;

and no deduction shall be allowed with respect to such interest (even if such deduction is not disallowed under subparagraphs (A) and (B))—

(C) if such interest is to be acquired for the surviving spouse, pursuant to directions of the decedent, by his executor or by the trustee of a trust.

For purposes of this paragraph, an interest shall not be considered as an interest which will terminate or fail merely because it is the ownership of a bond, note, or similar contractual obligation, the discharge of which would not have the effect of an annuity for life or for a term.

* * * * *

(5) *Life estate with power of appointment in surviving spouse.*—In the case of an interest in property passing from the decedent, if his surviving spouse is entitled for life to all the income from the entire interest, or all the income from a specific portion thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the interest, or such specific portion, to any person other than the surviving spouse—

(A) the interest or such portion thereof so passing shall, for purposes of subsection (a), be considered as passing to the surviving spouse, and

(B) no part of the interest so passing shall, for purposes of paragraph (1)(A), be considered as passing to any person other than the surviving spouse.

This paragraph shall apply only if such power in the surviving spouse to appoint the entire interest, or such specific portion thereof, whether exercisable by will or during life, is exercisable by such spouse alone and in all events.

(6) *Life insurance or annuity payments with power of appointment in surviving spouse.*—In the case of an interest in property passing from the decedent consisting of proceeds under a life insurance, endowment, or annuity contract, if under the terms of the contract such proceeds are payable in installments or are held by the insurer subject to an agreement to pay interest thereon (whether the proceeds, on the termination of any interest payments, are payable in a lump sum or in annual or more frequent installments), and such installment or interest payments are payable annually or at more frequent intervals, commencing not later than 13 months after the decedent's death, and all amounts, or a specific portion of all such amounts, payable during the life of the surviving spouse are payable only to such spouse, and such spouse has the power to appoint all amounts, or such specific portion, payable under such contract (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), with no power in any other person to appoint such amounts to any person other than the surviving spouse—

(A) such amounts shall, for purposes of subsection (a), be considered as passing to the surviving spouse, and

(B) no part of such amounts shall, for purposes of paragraph (1)(A), be considered as passing to any person other than the surviving spouse.

This paragraph shall apply only if, under the terms of the contract, such power in the surviving spouse to appoint such amounts, whether exercisable by will or during life, is exercisable by such spouse alone and in all events.

(c) *Limitation on Aggregate of Deductions.*—

(1) *General rule.*—The aggregate amount of the deductions allowed under this section (computed without regard to this subsection) shall not exceed 50 percent of the value of the adjusted gross estate, as defined in paragraph (2).

* * * * * *

Treasury Regulations on Estate Tax (1954 Code) (26 C.F.R.):

SEC. 20.2056(b)-5. *Marital deduction; life estate with power of appointment in surviving spouse.*

(a) *In general.* Section 2056(b)(5) provides that if an interest in property passes from the decedent to his surviving spouse (whether or not in trust) and the spouse is entitled for life to all the income from the entire interest or all the income from a specific portion of the entire interest, with a power in her to appoint the entire interest or the specific portion, the interest which passes to her is a deductible interest, to the extent that it satisfies all five of the conditions set forth below (see paragraph (b) of this section if one or more of the conditions is satisfied as to only a portion of the interest):

(1) The surviving spouse must be entitled for life to all of the income from the entire interest or a specific portion of the entire interest, or to a specific portion of all the income from frequent intervals.

(2) The income payable to the surviving spouse must be payable annually or at more frequent intervals.

(3) The surviving spouse must have the power to appoint the entire interest or the specific portion to either herself or her estate.

(4) The power in the surviving spouse must be exercisable by her alone and (whether exercisable by will or during life) must be exercisable in all events.

(5) The entire interest or the specific portion must not be subject to a power in any other person to appoint any part to any person other than the surviving spouse.

(b) *Specific portion; deductible amount.* If either the right to income or the power of appointment passing to the surviving spouse pertains only to a specific portion of a property interest passing from the decedent, the marital deduction is allowed only to the extent that the rights in the surviving spouse meet all of the five conditions described in paragraph (a) of this section. While the rights over the income and the power must coexist as to the same interest in property, it is not necessary that the rights over the income or the power as to such interest be in the same proportion. However, if the rights over income meeting the required conditions set forth in paragraph (a)(1) and (2) of this section extend over a smaller share of the property interest than the share with respect to which the power of appointment requirements set forth in paragraph (a)(3) through (5) of this section are satisfied, the deductible interest is limited to the smaller share. Correspondingly, if a power of appointment meeting all the requirements extends to a smaller portion of the property interest than the portion over which the income rights pertain, the deductible interest cannot exceed the value of the portion to which such power of appointment applies. Thus, if the decedent leaves to his surviving spouse the right to receive annually all of the income from a particular property interest and a power of appointment meeting the specifications prescribed in paragraph (a)(3) through (5) of this section as to only one-half of the property inter-

est, then only one-half of the property interest is treated as a deductible interest. Correspondingly, if the income interest of the spouse satisfying the requirements extends to only one-fourth of the property interest and a testamentary power of appointment satisfying the requirements extends to all of the property interest, then only one-fourth of the interest in the spouse qualifies as a deductible interest. Further, if the surviving spouse has no right to income from a specific portion of a property interest but a testamentary power of appointment which meets the necessary conditions over the entire interest, then none of the interest qualifies for the deduction. In addition, if, from the time of the decedent's death, the surviving spouse has a power of appointment meeting all of the required conditions over three-fourths of the entire property interest and the prescribed income rights over the entire interest, but with a power in another person to appoint one-half of the entire interest, the value of the interest in the surviving spouse over only one-half of the property interest will qualify as a deductible interest.

(c) *Definition of "specific portion"*. A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse in income and as to the power constitute a fractional or percentile share of a property interest so that such interest or share in the surviving spouse reflects its proportionate share of the increment or decline in the whole of the property interest to which the income rights and the power relate. Thus, if the right of the spouse to income and the power extend to one-half or a specified percentage of the property, or the equivalent, the interest is considered as a specific portion. On the other hand, if the annual income of the spouse is limited to a specific sum, or if she has

a power to appoint only a specific sum out of a larger fund, the interest is not a deductible interest. Even though the rights in the surviving spouse may not be expressed in terms of a definite fraction or percentage, a deduction may be allowable if it is shown that the effect of local law is to give the spouse rights which are identical to those she would have acquired if the size of the share had been expressed in terms of a definite fraction or percentage. The following examples illustrate the application of this and the preceding paragraphs of this section:

Example (*1*). The decedent transferred to a trustee 500 identical shares of X Company stock. He provided that during the lifetime of the surviving spouse the trustee should pay her annually one-half of the trust income or $6,000, whichever is the larger. The spouse was also given a general power of appointment, exercisable by her last will over the sum of $160,000 or over three-fourths of the trust corpus, whichever should be of larger value. Since there is no certainty that the trust income will not vary from year to year, for purposes of paragraphs (a) and (b) of this section, an annual payment of a specified sum, such as the $6,000 provided for in this case, is not considered as representing the income from a definite fraction or a specific portion of the entire interest if that were the extent of the spouse's interest. However, since the spouse is to receive annually at least one-half of the trust income, she will, for purposes of paragraphs (a) and (b) of this section, be considered as receiving all of the income from one-half of the entire interest in the stock. Inasmuch as there is no certainty that the value of the stock will be the same on the date of the surviving spouse's death as it was on the date of the decedent's death, for purposes of paragraphs (a) and (b) of this section, a specified sum, such as the $160,000 provided for in this case, is not considered to be a

definite fraction of the entire interest. However, since the surviving spouse has a general power of appointment over at least three-fourths of the trust corpus, she is considered as having a general power of appointment over three-fourths of the entire interest in the stock.

Example (2). The decedent bequeathed to a trustee an office building and 250 identical shares of Y Company stock. He provided that during the lifetime of the surviving spouse the trustee should pay her annually three-fourths of the trust income. The spouse was given a general power of appointment, exercisable by will, over the office building and 100 shares of the stock. By the terms of the decedent's will the spouse is given all the income from a definite fraction of the entire interest in the office building and in the stock. She also has a general power of appointment over the entire interest in the office building. However, since the amount of property represented by a single share of stock would be altered if the corporation split its stock, issued stock dividends, made a distribution of capital, etc., a power to appoint 100 shares at the time of the surviving spouse's death is not the same necessarily as a power to appoint 100/250 of the entire interest which the 250 shares represented on the date of the decedent's death. If it is shown in this case that the effect of local law is to give the spouse a general power to appoint not only the 100 shares designated by the decedent but also 100/250 of any shares or amounts which are distributed by the corporation and included in the corpus, the requirements of this paragraph will be satisfied and the surviving spouse will be considered as having a general power to appoint 100/250 of the entire interest in the 250 shares.

(d) *Definition of "entire interest".* Since a marital deduction is allowed for each qualifying separate interest in property passing

from the decedent to his surviving spouse (subject to the percentage limitation contained in §§ 20.2056(c)–1 and 20.2056(c)–2 concerning the aggregate amount of the deductions), for purposes of paragraphs (a) and (b) of this section, each property interest with respect to which the surviving spouse received some rights is considered separately in determining whether her rights extend to the entire interest or to a specific portion of the entire interest. A property interest which consists of several identical units of property (such as a block of 250 shares of stock, whether the ownership is evidenced by one or several certificates) is considered one property interest, unless certain of the units are to be segregated and accorded different treatment, in which case each segregated group of items is considered a separate property interest. The bequest of a specified sum of money constitutes the bequest of a separate property interest if immediately following distribution by the executor and thenceforth it, and the investments made with it, must be so segregated or accounted for as to permit its identification as a separate item of property. The application of this paragraph may be illustrated by the following examples:

Example (1). The decedent transferred to a trustee three adjoining farms, Blackacre, Whiteacre, and Greenacre. His will provided that during the lifetime of the surviving spouse the trustee should pay her all of the income from the trust. Upon her death, all of Blackacre, a one-half interest in Whiteacre, and a one-third interest in Greenacre were to be distributed to the person or persons appointed by her in her will. The surviving spouse is considered as being entitled to all of the income from the entire interest in Blackacre, all of the income from the entire interest in Whiteacre, and all of the income from the entire interest in Greenacre. She also is considered as hav-

ing a power of appointment over the entire interest in Blackacre, over one-half of the entire interest in Whiteacre, and over one-third of the interest in Greenacre.

Example (2). The decedent bequeathed $250,000 to C, as trustee. C is to invest the money and pay all of the income from the investments to W, the decedent's surviving spouse, annually. W was given a general power, exercisable by will, to appoint one-half of the corpus of the trust. Here, immediately following distribution by the executor, the $250,000 will be sufficiently segregated to permit its identification as a separate item, and the $250,000 will constitute an entire property interest. Therefore, W has a right to income and a power of appointment such that one-half of the entire interest is a deductible interest.

Example (3). The decedent bequeathed 100 shares of Z Corporation stock to D, as trustee. W, the decedent's surviving spouse, is to receive all of the income of the trust annually and is given a general power, exercisable by will, to appoint out of the trust corpus the sum of $25,000. In this case the $25,000 is not, immediately following distribution, sufficiently segregated to permit its identification as a separate item of property in which the surviving spouse has the entire interest. Therefore, the $25,000 does not constitute the entire interest in a property for the purpose of paragraphs (a) and (b) of this section.

(e) *Application of local law.* In determining whether or not the conditions set forth in paragraph (a)(1) through (5) of this section are satisfied by the instrument of transfer, regard is to be had to the applicable provisions of the law of the jurisdiction under which the interest passes and, if the transfer is in trust, the applicable provisions of the law governing the administration of the trust. For example, silence of a trust instrument as to the frequency

of payment will not be regarded as a failure to satisfy the condition set forth in paragraph (a)(2) of this section that income must be payable to the surviving spouse annually or more frequently unless the applicable law permits payment to be made less frequently than annually. The principles outlined in this paragraph and paragraphs (f) and (g) of this section which are applied in determining whether transfers in trust meet such conditions are equally applicable in ascertaining whether, in the case of interests not in trust, the surviving spouse has the equivalent in rights over income and over the property.

(f) *Right to income.* (1) If an interest is transferred in trust, the surviving spouse is "entitled for life to all of the income from the entire interest or a specific portion of the entire interest," for the purpose of the condition set forth in paragraph (a)(1) of this section, if the effect of the trust is to give her substantially that degree of beneficial enjoyment of the trust property during her life which the principles of the law of trusts accord to a person who is unqualifiedly designated as the life beneficiary of a trust. Such degree of enjoyment is given only if it was the decedent's intention, as manifested by the terms of the trust instrument and the surrounding circumstances, that the trust should produce for the surviving spouse during her life such an income, or that the spouse should have such use of the trust property as is consistent with the value of the trust corpus and with its preservation. The designation of the spouse as sole income beneficiary for life of the entire interest or a specific portion of the entire interest will be sufficient to qualify the trust unless the terms of the trust and the surrounding circumstances considered as a whole evidence an intention to deprive the spouse of the requisite degree of enjoyment. In determining whether a trust

evidences that intention, the treatment required or permitted with respect to individual items must be considered in relation to the entire system provided for the administration of the trust.

* * * * *

SEC. 20.2056(b)–6. *Marital deduction; life insurance or annuity payments with power of appointment in surviving spouse.*

(a) *In general.* Section 2056(b)(6) provides that an interest in property passing from a decedent to his surviving spouse, which consists of proceeds held by an insurer under the terms of a life insurance, endowment, or annuity contract, is a "deductible interest" to the extent that it satisfied all five of the following conditions (see paragraph (b) of this section if one or more of the conditions is satisfied as to only a portion of the proceeds):

(1) The proceeds, or a specific portion of the proceeds, must be held by the insurer subject to an agreement either to pay the entire proceeds or a specific portion thereof in installments, or to pay interest thereon, and all or a specific portion of the installments or interest payable during the life of the surviving spouse must be payable only to her.

(2) The installments or interest payable to the surviving spouse must be payable annually, or more frequently, commencing not later than 13 months after the decedent's death.

(3) The surviving spouse must have the power to appoint all or a specific portion of the amounts so held by the insurer to either herself or her estate.

(4) The power in the surviving spouse must be exercisable by her alone and (whether exercisable by will or during life) must be exercisable in all events.

(5) The amounts or the specific portion of the amounts payable under such contract must

not be subject to a power in any other person to appoint any part thereof to any person other than the surviving spouse.

(b) *Specific portion; deductible interest.* If the right to receive interest or installment payments or the power of appointment passing to the surviving spouse pertains only to a specific portion of the proceeds held by the insurer, the martial deduction is allowed only to the extent that the rights of the surviving spouse in the specific portion meet the five conditions described in paragraph (a) of this section. While the rights to interest, or to receive payment in installments, and the power must coexist as to the proceeds of the same contract, it is not necessary that the rights to each be in the same proportion. If the rights to interest meeting the required conditions set forth in paragraph (a)(1) and (2) of this section extend over a smaller share of the proceeds than the share with respect to which the power of appointment requirements set forth in paragraph (a) (3) through (5) of this section are satisfied, the deductible interest is limited to the smaller share. Similarly, if the portion of the proceeds payable in installments is a smaller portion of the proceeds than the portion to which the power of appointment meeting such requirements relates, the deduction is limited to the smaller portion. In addition, if a power of appointment meeting all the requirements extends to a smaller portion of the proceeds than the portion over which the interest or installment rights pertain, the deductible interest cannot exceed the value of the portion to which such power of appointment applies. Thus, if the contract provides that the insurer is to retain the entire proceeds and pay all of the interest thereon annually to the surviving spouse and if the surviving spouse has a power of appointment meeting the specifications pre-

scribed in paragraph (a)(3) through (5) of this section, as to only one-half of the proceeds held, then only one-half of the proceeds may be treated as a deductible interest. Correspondingly, if the rights of the spouse to receive installment payments or interest satisfying the requirements extend to only one-fourth of the proceeds and a testamentary power of appointment satisfying the requirements of paragraph (a)(3) through (5) of this section extends to all of the proceeds, then only one-fourth of the proceeds qualifies as a deductible interest. Further, if the surviving spouse has no right to installment payments (or interest) over any portion of the proceeds but a testamentary power of appointment which meets the necessary conditions over the entire remaining proceeds, then none of the proceeds qualifies for the deduction. In addition, if, from the time of the decedent's death, the surviving spouse has a power of appointment meeting all of the required conditions over three-fourths of the proceeds and the right to receive interest from the entire proceeds, but with a power in another person to appoint one-half of the entire proceeds, the value of the interest in the surviving spouse over only one-half of the proceeds will qualify as a deductible interest.

(c) *Applicable principles.* (1) The principles set forth in paragraph (c) of § 20.2056(b)–5 for determining what constitutes a "specific portion of the entire interest" for the purpose of section 2056(b)(5) are applicable in determining what constitutes a "specific portion of all such amounts" for the purpose of section 2056(b)(6). However, the interest in the proceeds passing to the surviving spouse will not be disqualified by the fact that the installment payments or interest to which the spouse is entitled or the amount of the proceeds over which

the power of appointment is exercisable may be expressed in terms of a specific sum rather than a fraction or a percentage of the proceeds provided it is shown that such sums are a definite or fixed percentage or fraction of the total proceeds.

(2) The provisions of paragraph (a) of this section are applicable with respect to a property interest which passed from the decedent in the form of proceeds of a policy of insurance upon the decedent's life, a policy of insurance upon the life of a person who predeceased the decedent, a matured endowment policy, or an annuity contract, but only in case the proceeds are to be held by the insurer. With respect to proceeds under any such contract which are to be held by a trustee, with power of appointment in the surviving spouse, see § 20.2056(b)–5. As to the treatment of proceeds not meeting the requirements of § 20.2056(b)–5 or of this section, see § 20.2056(a)–2.

(3) In the case of a contract under which payments by the insurer commenced during the decedent's life, it is immaterial whether or not the conditions in subparagraphs (1) through (5) of paragraph (a) of this section were satisfied prior to the decedent's death.

(d) *Payments of installments or interest.* The conditions in subparagraphs (1) and (2) of paragraph (a) of this section relative to the payments of installments or interest to the surviving spouse are satisfied if, under the terms of the contract, the spouse has the right exercisable annually (or more frequently) to require distribution to herself of installments of the proceeds or a specific portion thereof, as the case may be, and otherwise such proceeds or interest are to be accumulated and held by the insurer pursuant to the terms of the contract. A contract which otherwise requires the insurer to make annual or more frequent pay-

ments to the surviving spouse following the decedent's death, will not be disqualified merely because the surviving spouse must comply with certain formalities in order to obtain the first payment. For example, the contract may satisfy the conditions in subparagraphs (1) and (2) of paragraph (a) of this section even though it requires the surviving spouse to furnish proof of death before the first payment is made. The condition in paragraph (a)(1) of this section is satisfied where interest on the proceeds or a specific portion thereof is payable, annually or more frequently, for a term, or until the occurrence of a specified event, following which the proceeds or a specific portion thereof are to be paid in annual or more frequent installments.

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U.S. GOVERNMENT PRINTING OFFICE: 1967

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SUPREME COURT OF THE UNITED STATES

No. 637.—October Term, 1966.

Northeastern Pennsylvania National Bank & Trust Company, Petitioner, *v.* United States.	On Writ of Certiorari to the United States Court of Appeals for the Third Circuit.

[May 22, 1967.]

Mr. Justice Fortas delivered the opinion of the Court.

The issue in this case is whether a bequest in trust providing for the monthly payment to decedent's widow of a fixed amount can qualify for the estate tax marital deduction under § 2056 (b) 5 of the Internal Revenue Code of 1954. That section allows a marital deduction from a decedent's adjusted gross estate of up to one-half the value of the estate in respect to specified interests which pass to the surviving spouse. Among the interests which qualify is one in which the surviving spouse "is entitled for life to . . . all the income from a specific portion [of the trust property], payable annually or at more frequent intervals, with power in the surviving spouse to appoint . . . such specific portion . . . ."[1]

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[1] The section reads, in full:

"(5) *Life estate with power of appointment in surviving spouse.*—In the case of an interest in property passing from the decedent, if his surviving spouse is entitled for life to all the income from the entire interest, or all the income from a specific portion thereof, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire interest, or such specific portion (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the

At the date of decedent's death, the value of the trust corpus created by his will was $69,246. The will provided that his widow should receive $300 per month until decedent's youngest child reached 18, and $350 per month thereafter. If the trust income were insufficient, corpus could be invaded to make the specified payments; if income exceeded the monthly amount, it was to be accumulated. The widow was given power to appoint the entire corpus by will.[2]

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interest, or such specific portion, to any person other than the surviving spouse—

"(A) the interest or such portion thereof so passing shall, for purposes of subsection (a), be considered as passing to the surviving spouse, and

"(B) no part of the interest so passing shall, for purposes of paragraph (1)(A), be considered as passing to any person other than the surviving spouse.

"This paragraph shall apply only if such power in the surviving spouse to appoint the entire interest, or such specific portion thereof, whether exercisable by will or during life, is exercisable by such spouse alone and in all events."

[2] The trustee was also given discretion to invade up to $1,500 of corpus in the event of the widow's illness or financial emergency. The relevant part of the will is as follows:

"ITEM 6. I give, devise and bequeath one-half (½) of all the rest, residue and remainder of my estate, whatsoever and wheresoever the same be, both real and personal, to which I may be entitled, or which I may have power to dispose of at the time of my death, unto my Trustee hereinafter named and designated, to have and to hold the same in trust, nevertheless, as hereinafter provided.

"(a) I direct my Trustee to pay out of the said income and corpus of the said estate unto my wife, Beatrice O. Young, the sum of Three Hundred Dollars ($300.00) per month for and during the period until my youngest child reaches the age of eighteen years, and thereafter I direct my Trustee to pay my wife, Beatrice O. Young, the sum of Three Hundred Fifty Dollars ($350.00) per month for and during the rest of her natural life.

"(b) If my wife survives me, she shall have the power, exercisable by Will, to appoint to her estate, or to others, any or all of the

On decedent's estate tax return, his executor reported an adjusted gross estate of $199,750. The executor claimed the maximum marital deduction of one-half the gross estate, $99,875, on the ground that qualified interests passing to the wife exceeded that amount. The value of the property which passed to the widow outright was $41,751. To this the executor added the full value of the trust, $69,246. The Commissioner, however, determined that the trust did not qualify for the marital deduction because the widow's right to the income of the trust was not expressed as a "fractional or percentile share" of the total trust income, as the Treasury Regulations § 20.2056 (b)–5 (c), require. Accordingly, the Commissioner reduced the amount of the allowable deduction to $41,751. The resulting deficiency in estate tax was paid, a claim for refund was disallowed, the executor sued in District Court for refund, and the District Judge gave summary judgment for the executor. On appeal, the Court of Appeals for the Third Circuit, sitting *en banc*, reversed, with three judges dissenting. Because of an acknowledged conflict between the decision of the Third Circuit in this case and that of the Seventh Circuit in *United States* v. *Citizens National Bank of Evansville*, 359 F. 2d 817, petition for certiorari pending, No. 488, October Term, 1966,[3] we granted certiorari. — U. S. —. We reverse.

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principal remaining at the time of her death. If my wife fails to appoint the entire principal to her estate or to others as above authorized, then upon her death (or if she predeceases me, then upon my death) any principal remaining at the time shall be paid over to my children on the same terms and conditions as under Item 7 of this my Will."

[3] In the *Citizens National Bank* case, decedent directed the trustee to pay the surviving wife $200 per month for the two years following his death, and thereafter $300 per month; the widow was the sole beneficiary. The District Director disallowed that part of the executor-bank's claim to an estate tax marital deduction based upon

The basis for the Commissioner's disallowance lay in Treasury Regulations § 20.2056 (b)–5 (c). This interpretative Regulation purports to define "specific portion" as it is used in § 2056 (b)–5 of the Code: "A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse in income . . . constitute a fractional or percentile share of a property interest . . . ." The Regulation specifically provides that "if the annual income of the spouse is limited to a specific sum . . . the interest is not a deductible interest."[4] If this Regulation properly

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the trust, and the bank sued for a refund. The District Court held in favor of the bank, and computed the allowable deduction by capitalizing the $200 monthly stipend at an assumed 3½% rate of return. The Court of Appeals affirmed, one judge dissenting.

The decision of the Court of Appeals for the Third Circuit in the present case is also in apparent conflict with a decision of the Court of Appeals for the Second Circuit in *Gelb* v. *Commissioner,* 298 F. 2d 544 (1962) (Friendly, J.). The surviving widow in *Gelb* was entitled to all the income from the trust. The trustees (of which the wife was one) were empowered to invade corpus up to $5,000 per year for the education and support of testator's youngest daughter, the payments to be made to the wife. The Court of Appeals held that the present worth of the maximum amount payable to the daughter could be computed actuarially, taking into account the joint expectancy of the widow and daughter, and could then be deducted from the total trust corpus to arrive at the "specific portion" as to which the widow was given a power of appointment. The Court of Appeals observed that "Congress spoke of a 'specific portion,' not of a 'fractional or percentile share . . . .' " 298 F. 2d, at 550–551, and disapproved the Regulation "insofar as it would limit a 'specific portion' to 'a fractional or percentile share.' " 298 F. 2d, at 551.

[4] The relevant part of the Regulation is as follows:

"(c) *Definition of 'specific portion.'* A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse in income and as to the power constitute a fractional or percentile share of a property interest so that such interest or share in the surviving spouse reflects its pro-

implements the Code, the trust in this case plainly fails to qualify for the marital deduction. We hold, however, that in the context of this case the Regulation improperly restricts the scope of the congressionally granted deduction.

In the District Court, the executor initially claimed that the entire trust qualified for the marital deduction simply because, at the time of trial, the corpus had not yet produced an income in excess of $300 per month, and that the widow was therefore entitled "to all the income from the entire interest." The District Court rejected this contention, observing that the income from the corpus *could* exceed $300 per month, and in that event the excess would have to be accumulated. The executor's alternative claim, which the District Court accepted, was that the "specific portion" of the trust corpus whose income would amount to $300 per month could be computed, and a deduction allowed for that amount.[5]

Resolution of the question in this case, whether a qualifying "specific portion" can be computed from the monthly stipend specified in a decedent's will, is essentially a matter of discovering the intent of Congress. The general history of the marital deduction is well known. See *United States* v. *Stapf*, 375 U. S. 118, 128

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portionate share of the increment or decline in the whole of the property interest to which the income rights and the power relate. Thus, if the right of the spouse to income and the power extend to one-half or a specified percentage of the property, or the equivalent, the interest is considered as a specific portion. On the other hand, if the annual income of the spouse is limited to a specific sum, or if she has a power to appoint only a specific sum out of a larger fund, the interest is not a deductible interest."

[5] Because the marital deduction is computed as of the date of the deceased spouse's death, *Jackson* v. *United States*, 376 U. S. 503, 508 (1964), the parties are agreed that the monthly stipend to be considered is $300 per month, not $350 per month.

(1963). The deduction was enacted in 1948, and the underlying purpose was to equalize the incidence of the estate tax in community property and common-law jurisdictions. Under a community property system a surviving spouse takes outright ownership of half of the community property, which therefore is not included in the deceased spouse's estate. The marital deduction allows transfer of up to one-half of noncommunity property to the surviving spouse free of the estate tax. Congress, however, allowed the deduction even when the interest transferred is less than the outright ownership which community property affords. In "recognition of one of the customary modes of transfer of property in common-law States,"[6] the 1948 statute provided that a bequest in trust, with the surviving spouse "entitled for life to all the income from the corpus of the trust, payable annually or at more frequent intervals, with power . . . to appoint the entire corpus"[7] would qualify for the deduction.

The 1948 legislation required that the bequest in trust entitle the surviving spouse to "all the income" from the trust corpus, and grant a power to appoint the "entire corpus." These requirements were held by several lower courts to disqualify for the deduction a single trust in which the surviving spouse was granted a right to receive half (for example) of the income and to appoint half of the corpus.[8] Since there was no good reason to require a testator to create two separate trusts—one for his wife,

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[6] S. Rep. No. 1013, 80th Cong., 2d Sess. (1948), p. 28.

[7] Internal Revenue Code of 1939, § 812 (e)(1)(F), as added by § 361 of the Revenue Act of 1948, c. 168, 62 Stat. 117.

[8] See, *e. g., Estate of Shedd* v. *Commissioner,* 237 F. 2d 345 (C. A. 9th Cir.), cert. denied, 352 U. S. 1024 (1957); *Estate of Sweet* v. *Commissioner,* 234 F. 2d 401 (C. A. 10th Cir.), cert. denied, 352 U. S. 878 (1956). See also S. Rep. No. 1983, 85th Cong., 2d Sess. (1958), pp. 240–241.

the other for his children, for example—Congress in 1954 revised the marital deduction provision of the statute to allow the deduction where a decedent gives his surviving spouse "all the income from the entire interest, or all the income from a specific portion thereof" and a power to "appoint the entire interest, or such specific portion." The House Report on this change states that "The bill makes it clear that . . . a right to income plus a general power of appointment over only an undivided part of the property will qualify that part of the property for the marital deduction."[9] The Senate Report contains identical language.[10] There is no indication in the legislative history of the change from which one could conclude that Congress—in using the words "all the income from a specific portion" in the statute, or the equivalent words "a right to income . . . over . . . an undivided part" in the committee reports—intended that the deduction afforded would be defeated merely because the "specific portion" or the "undivided part" was not expressed by the testator in terms of a "fractional or percentile share" of the whole corpus.[11]

Congress' intent to afford a liberal "estate-splitting" possibility to married couples, where the deductible half of the decedent's estate would ultimately—if not consumed—be taxable in the estate of the survivor, is unmistakable. Indeed, in § 93 of the Technical Amend-

[9] H. R. Rep. No. 1337, 83d Cong., 2d Sess. (1954), p. 92.

[10] S. Rep. No. 1622, 83d Cong., 2d Sess. (1954), p. 125.

[11] To be sure, the two reports do give an example of the simplest kind of trust covered by the change: "For example, if the decedent in his will provided for the creation of a trust under the terms of which the income from one-half of the trust property is payable to this surviving spouse with uncontrolled power in the spouse to appoint such one-half of the trust property by will, such interest will qualify. . . ." Reports, *supra*, notes 9 and 10, at A319, 475, respectively. Obviously this example was not intended to limit the meaning of the new language.

ments Act of 1958, 72 Stat. 1668, Congress made "The more realistic rules of the 1954 Code" apply retroactively to the original enactment of the marital deduction in 1948, and opened the statute of limitations to allow refunds or credits for over-payments.[12] Plainly such a provision should not be construed so as to impose unwarranted restrictions upon the the availability of the deduction. Yet the Government insists that even where there are well-established principles for computing the principal required to produce the monthly stipend provided for in a trust, a "specific portion" cannot be determined in that way. The "specific portion" must, the Government urges, be expressed in the trust as a fractional or percentile share of the total corpus. The spouse of a testator whose will provides for a specific monthly stipend is deprived of any benefit from the marital deduction, according to the Government's view. But we can find no warrant for that narrow view, in commonsense or in the statute and its history.

The Government puts most of its reliance upon a phrase which occurred once in the legislative history of the 1948 enactment. The Senate Report stated that the marital deduction would be available "where the surviving spouse, by reason of her [*sic*] right to the income and a power of appointment, is the virtual owner of the property." [13] The Government's argument is that the deduction was intended only in cases where the equivalent of the outright ownership of a community property State was granted, and that this is what the Senate Report meant by the words "virtual owner." Actually, however, the words were not used in that context at all. The section of the Report from which those words derive deals with the rule that, with minor exceptions, the

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[12] S. Rep. No. 1983, 85th Cong., 2d Sess. (1958), p. 107.

[13] S. Rep. No. 1013, 80th Cong., 2d Sess., pt. 2 (1948), p. 16.

marital deduction does not apply where any person other than the surviving spouse has any power over the income or corpus of the trust. It is in this sense that the Report described the surviving spouse as a "virtual owner." Hence, the Government's argument that only a grant of the income from a fractional or percentile share subjects the surviving spouse to the vagaries and fluctuations of the economic performance of the corpus in the way an outright owner would be, is simply irrelevant. There is no indication whatsoever that Congress intended the deduction only to be available in such a situation, nor is there any apparent connection between the purposes of the deduction and such a limitation on its availability. Compare *Gelb* v. *Commissioner,* 298 F. 2d 544, 550–551 (C. A. 2d Cir. 1962). Obviously Congress did not intend the deduction to be available only with respect to interests equivalent to outright ownership, or trusts would not have been permitted to qualify at all.[14]

The Court of Appeals advanced a somewhat different argument in support of the Government's conclusion. Without relying upon the validity of the Regulation, the Court of Appeals maintained that a "specific portion" can be found only where there is an acceptable method of computing it, and that no such method is available in a case of the present sort. The Court of Appeals noted that the computation must produce the "ratio between the maximum monthly income [producible by the whole corpus] and the monthly stipend [provided for in the trust]." The following example was given:

> "If the investment factors involved were constant and it could be determined that the *maximum* income that could be produced from the corpus in a month was, for example, $500, then the relationship between the $300 monthly stipend and the $500

[14] Cf. Note, 19 Stan. L. Rev. 468, 470–472 (1967).

maximum income would define 'specific portion' for marital deduction purposes, *i. e.*:

> $300 being 3/5 of $500 then 3/5 of $69,245.85 would be the 'specific portion' of the trust corpus from which the surviving spouse would be entitled to the entire income of $300 monthly *under maximum production circumstances.*

"Though in reality it might take the entire corpus to produce the monthly stipend, or even the necessity to invade corpus might be present, nevertheless . . . it could be said, after computing the theoretical maximum income, that the surviving spouse's income interest of $300 monthly represented the investment of 3/5 of the corpus. 'Specific portion' would then be accurately defined for marital deduction purposes." (Italics in original.)

The Court of Appeals concluded, however, that the computation could not be made because "the market conditions for purposes of investment are not known" and, therefore, there are no constant investment factors to use in computing the maximum possible monthly income of the whole corpus.

It is with this latter conclusion that we disagree. To be sure, perfect prediction of realistic future rates of return [15] is not possible. However, the use of projected rates of return in the administration of the federal tax laws is hardly an innovation. Cf. *Gelb* v. *Commissioner*, 298 F. 2d 544, 551, n. 7 (C. A. 2d Cir. 1962). It should not be a difficult matter to settle on a rate of return

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[15] An estimated realistic rate of return which a trustee could be expected to obtain under reasonable investment conditions must be used—absent specific restrictions upon the trustee's investment powers—in order to isolate that "part of the corpus which in [all] . . . reasonable event[s]" will produce no more than the monthly stipend, to paraphrase the court below.

available to a trustee under reasonable investment conditions, which could be used to compute the "specific portion" of the corpus whose income is equal to the monthly stipend provided for in the trust. As the Court of Appeals for the Second Circuit observed in *Gelb, supra,* "the use of actuarial tables for dealing with estate tax problems has been so widespread and of such long standing that we cannot assume Congress would have balked at it here; the United States is in business with enough different taxpayers so that the law of averages has ample opportunity to work." 298 F. 2d, at 551–552.

The Government concedes, as it must, that application of a projected rate of return to determine the "specific portion" of the trust corpus whose income is equal to the monthly stipend allotted will not result in any of the combined marital estate escaping ultimate taxation in either the decedent's or the surviving spouse's estate. The Government argues, however, that if analogous actuarial methods were used to compute as a fixed dollar amount the "specific portion" as to which a qualifying power of appointment is given, where the power in fact granted extends to the whole corpus but the corpus is subject to measurable invasions for the benefit, for example, of a child, the result, in some cases, would be to enable substantial avoidance of estate tax. Whether, properly viewed, the Government's claim holds true, and, if so, what effect that should have upon the qualification of such a trust, is a difficult matter. Needless to say, nothing we hold in this opinion has reference to that quite different problem, which is not before us. Cf. *Gelb v. Commissioner, supra.*

The District Court used an annuity-valuation approach to compute the "specific portion." This was incorrect. The question, as the Court of Appeals recognized, is to determine the amount of the corpus required to produce

the fixed monthly stipend, not to compute the present value of the right to monthly payments over an actuarially computed life expectancy. Accordingly, we reverse and remand for further proceedings in conformity with this opinion.

Reversed.

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No. 637.—October Term, 1966.

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Mr. Justice Stewart, whom Mr. Justice Black and Mr. Justice Harlan join, dissenting.

"Resolution of the question in this case, whether a qualifying 'specific portion' can be computed from the monthly stipend specified in a decedent's will, is," says the Court, "essentially a matter of discovering the intent of Congress." P. 5, *ante*. Substituting "exclusively" for "essentially," I entirely agree with the Court's statement of the case. "The deduction was enacted in 1948, and the underlying purpose was to equalize the incidence of the estate tax in community property and common-law jurisdictions." P. 6, *ante*. Again I agree. But I must differ with the Court in its determination that the intent of Congress leads to the result the Court today reaches. For allowing the trust before us to qualify for the marital deduction will inevitably lead to the ironic and unjustified result of giving common-law jurisdictions more favorable tax treatment than community property States.

The Court holds that the widow in this case had an interest in "all the income from a specific portion" of the trust because the stream of payments to her could be capitalized by the use of assumed interest rates. This capitalized sum is then said to constitute the "specific portion" which qualifies for the marital deduction. A corollary of the Court's theory is that a trust which gave the widow the right to the income from a fixed amount

(in dollars) of corpus and the right to appoint the entire corpus would support a marital deduction.[1] But if such a bequest qualifies, then one which limits her power of appointment to only that amount of corpus with respect to which she has income rights will also qualify for the marital deduction. For under the statute, the survivor must have only the right to "all the income from a specific portion . . . with power in the surviving spouse to appoint . . . *such* specific portion."[2] (Emphasis added.) The way in which such an estate allows a tax avoidance scheme not available to a community-property couple can be easily illustrated.

Assume a trust estate of $200,000, with the widow receiving the right to the income from $100,000 of its corpus and a power of appointment over that $100,000, and the children of the testator receiving income from

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[1] The only difference between a trust which gives the wife income from a fixed amount of corpus and the one the Court has before it today is that the former does not require capitalizing a stream of payments into a lump sum, since it defines the sum at the outset. Neither of these trusts would qualify for the marital deduction under current Treasury Regulations:

"*Definition of 'specific portion.'* A partial interest in property is not treated as a specific portion of the entire interest unless the rights of the surviving spouse . . . constitute a fractional or percentile share of a property interest so that such interest or share . . . reflects its proportionate share of the increment or decline in the whole of the property interest . . . . [I]f the annual income of the spouse is limited to a specific sum, or if she has a power to appoint only a specific sum out of a larger fund, the interest is not a deductible interest." Treas. Reg. § 20.2056 (b)–5 (c).

[2] The Court describes the "specific portion" over which the wife has a power of appointment as involving a "quite different problem" from the question directly before us today. P. 11, *ante*. But unless it could be held that "such a specific portion" does not refer to "a specific portion" (and I do not see how such a holding is possible), the way in which the Court defines "specific portion" with regard to the survivor's income rights will inevitably affect the meaning of "specific portion" with regard to the power of appointment.

the balance of the corpus during the widow's life, their remainders to vest when she dies. Now suppose that when the widow dies the trust corpus has doubled in value to $400,000. The wife's power of appointment over $100,000 applies only to make $100,000 taxable to her estate.[3] The remaining $300,000 passes tax free to the children. Contrast the situation in a community property State. The wife's 50% interest in the community property places $200,000 of the expanded assets in her estate and taxable as such; only $200,000, therefore, passes directly to the children. Thus, the Court's interpretation of "specific portion" affords common-law estates a significant tax advantage that community property dispositions cannot obtain.

By changing "specific portion" from the fractional share, which is both described in the Treasury Regulation and used as the basis for community property ownership, into a lump sum bearing no constant relation to the corpus, the Court allows capital appreciation to be transferred from the wife's to the children's interest in the estate without any tax consequence. Thus, today's decision is directly opposed to what we have previously recognized as the purpose of the marital deduction:

> "The purpose . . . is only to permit a married couple's property to be taxed in two stages and not to allow a tax-exempt transfer of wealth into succeeding generations. Thus the marital deduction is generally restricted to the transfer of property interests that will be includible in the surviving spouse's gross estate." *United States* v. *Stapf*, 375 U. S. 118, 128.

The reference in the legislative history of the 1948 Act to the wife's "virtual owner[ship]" of the interest quali-

[3] Section 2041 of the Internal Revenue Code of 1954.

fying for the deduction is explained by the purpose discerned in *Stapf, supra.*[4] For only if she is the "virtual owner," will the wife's interest appreciate with the rest of the trust. Similarly, the congressional committee reports, in limiting their examples of "specific portions" to fractional shares, manifest an understanding that no tax avoidance was to be allowed via the marital deduction.[5] In no other manner could Congress have "equalize[d] the incidence of the estate tax in community property and common law jurisdictions," as the Court so aptly puts it.

In ruling as it does today the Court not only frustrates the basic purposes of the marital deduction; it also ignores or brushes aside guideposts for deciding tax cases that have been carefully established in prior decisions of this Court. Thus, a 10-year-old interpretation of the statute contained in the Treasury Regulations is held invalid, although we have consistently given great weight to those regulations in the interpretation of tax statutes. See, *e. g., United States* v. *Stapf,* 375 U. S. 118, 127, n. 11.

Of even greater importance is the sharp change of attitude toward the marital deduction which today's decision heralds. The Treasury's interpretation of "specific portion" is held invalid because "Congress' intent [was] to afford a liberal 'estate-splitting' possibility." This finding of "liberalism" in the marital deduction leads the Court to reason that "[p]lainly such a provision should not be construed so as to impose unwarranted restrictions upon the availability of the deduction." P. 7–8, *ante.* But we have previously construed the marital deduction to mean what it says and have not discerned a liberal intent that allows us to write new

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[4] S. Rep. No. 1013, Part 2, 80th Cong., 2d Sess. (1948), p. 16.

[5] H. R. Rep. No. 1337, 83d Cong., 2d Sess. (1954), p. A319; S. Rep. No. 1622, 83d Cong., 2d Sess. (1954), p. 475.

words into the statute, as the Court does here in changing "specific portion" to "ascertainable amount." For example, in *Jackson* v. *United States,* 376 U. S. 503, 510, eight members of the Court, speaking through MR. JUSTICE WHITE, declared that "the marital deduction . . . was knowingly hedged with limitations" by Congress, and "[t]o the extent it was thought desirable to modify the rigors of [such limitations], exceptions . . . were written into the Code." Thus, the lesson announced in *Jackson,* but ignored today, was that "[c]ourts should hesitate to provide [other exceptions] by straying so far from the statutory language." Cf. *Meyer* v. *United States,* 364 U. S. 410. One looks in vain through the *Jackson, Meyer,* and *Stapf* opinions, *supra,* for the roots of the liberalism which the Court today finds bursting forth from the marital deduction.

With this change in approach, uncertainty is now introduced into one of the areas of the law where long-range reliance upon the meaning of a statute is essential. Estate planners and tax lawyers are technicians schooled to view the marital deduction as a tightly drawn, precise provision. They are now shown a totally new statute that is to be construed in the manner of a workman's compensation act. See *Jackson* v. *Lykes Bros.,* —— U. S. ——. Such a construction will hardly promote "[t]he achievement of the purposes of the marital deduction [which] is dependent to a great degree upon the careful drafting of wills." *Jackson* v. *United States,* 376 U. S., at 511.

Believing today's decision to be at odds with the statutory purpose and the consistent interpretation of the marital deduction, I respectfully dissent.